Annual Report
2005–06

Independent Evaluation Office
International Monetary Fund

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Appendices

Abbreviations and Acronyms

BCP	Basle Core Principles
ECG	Evaluation Cooperation Group
BSR	Biennial Review of Surveillance
ECG	Evaluation Cooperation Group
FAD	Fiscal Affairs Department (IMF)
FSA	Financial Sector Assessment
FSAP	Financial Sector Assessment Program
FSLC	Financial Sector Liaison Committee
FSSA	Financial System Stability Assessment
GFSR	Global Financial Stability Report
IAIS	International Association of Insurance Supervisors
ICM	International Capital Markets Department (IMF)
IEG	Independent Evaluation Group (World Bank)
IEO	Independent Evaluation Office (IMF)
IF	Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries
IFI	International Financial Institution
IMF	International Monetary Fund
IMFC	International Monetary and Financial Committee
IOSCO	International Organization of Securities Commissions
JSA	Joint Staff Assessment
JSAN	Joint Staff Advisory Note
LOI	Letter of Intent
LTPE	Long-Term Program Engagement
MCM	Monetary and Capital Markets Department (IMF)
MDG	Millennium Development Goals
MEFP	Memorandum of Economic and Financial Policies
MFD	Monetary and Finance Department (IMF)
MTS	Medium-Term Strategy
OECD	Organization for Economic Cooperation and Development
OED	Operations Evaluation Department (World Bank)
OFC	Off-Shore Financial Center
PEM	Public Expenditure Management
PPM	Post Program Monitoring
PRGF	Poverty Reduction and Growth Facility
PRS	Poverty Reduction Strategy
PRSP	Poverty Reduction Strategy Paper
RAP	Resource Allocation Plans
ROSC	Report on the Observance of Standards and Codes

SA	Surveillance Agendas
SC	Structural Conditionality
TA	Technical Assistance
TACSN	TA Country Strategy Notes
TAIMS	TA Information Management System
TOR	Terms of Reference
WEO	World Economic Outlook

MESSAGE FROM THE DIRECTOR

This third *Annual Report,* the first under my tenure as Director of the IEO, describes the activities of the IEO during the past year and a half. We have aligned the time frame of the report with that of our fiscal and work program years. As a result, during this transitional year, developments over a period exceeding one calendar year are covered.

The last year has been a very important one in the history of the IEO. As envisaged at the time of the creation of the office, the fifth year of operation of the office coincided with a period of reflection about what had been achieved and what changes would help the IEO better fulfill its original mandate of increasing transparency and accountability, as well as strengthening the learning culture of the IMF. As part of that exercise, the Executive Board appointed an External Evaluation Panel and charged it with investigating whether the IEO is meeting its goals.

The Panel's report was discussed by the Executive Board in April 2006. Executive Directors agreed with the report that the IEO had served the IMF well and had earned strong support across a broad range of stakeholders. They also welcomed the Panel's observation that inside and outside interviewees were overwhelmingly of the view that the IEO has acted independently. Directors concurred that a more focused orientation, together with strong support from the Executive Board and Management would help ensure the IEO's continued usefulness and relevance. Chapter I of this *Annual Report* discusses the main findings and recommendations of the Evaluation Panel as well as the reactions of Executive Directors and describes concrete actions taken since then to follow up on the recommendations.

Chapter II of the *Annual Report* summarizes the findings and recommendations of five additional completed evaluations: on IMF Technical Assistance; the IMF's Approach to Capital Account Liberalization; IMF Support to Jordan, 1980–2004; the Financial Sector Assessment Program (FSAP); and Multilateral Surveillance. The status of three ongoing projects, on Structural Conditionality (SC) in IMF-Supported Program, on the Role of the IMF in Determining the External Financing Envelope in Sub-Saharan African Countries, and on IMF Advice on Exchange Rate Policy, is discussed in Chapter III. Finally, Chapter IV describes the recently approved work program for FY2007 and beyond, which adds four projects to the pipeline: Aspects of IMF Corporate Governance (including the role of the Executive Board), the IMF's Interactions with its Member Countries, the IMF's Research Agenda, and the IMF's Approach to International Trade Issues.

Important general lessons pertaining to strengthening IMF surveillance emerged from our two most recent evaluations which are particularly germane as the IMF implements its Medium-Term Strategy. The FSAP evaluation found that much improvement could be achieved in ensuring future coverage of all systemically important countries, in addressing cross-border issues and, more generally, in better integrating financial sector analysis with bilateral surveillance. The Multilateral Surveillance evaluation found that there is room to achieve a better integration of both financial and macroeconomic dimensions as well as bilateral and multilateral policy analysis and policy prescriptions. It called for a better "customer focus" in IMF products. This evaluation also stressed the need to enhance the impact of the Executive Board and the IMFC and smaller country groupings in multilateral surveillance activities.

Conducting effective evaluations of IMF activities is not possible without the cooperation of those being evaluated and feedback from capitals and external observers. I and the rest of the IEO staff would like to express our thanks to the Executive Board, IMF Management, and the staff for their time and responsiveness. At the same time, we would also express our appreciation to the many outside stakeholders who have shared their thoughts and perspectives with us.

Thomas A. Bernes
Director, IEO

I. Overview of Developments in Fiscal Years 2005 and 2006

The Independent Evaluation Office (IEO) was established by the Executive Board of the IMF in July 2001 to provide objective and independent evaluation on issues related to the IMF. The office operates independently of IMF management and at arm's length from the Executive Board. Its terms of reference emphasize the objectives of enhancing the learning culture within the IMF, strengthening the IMF's external credibility, promoting greater understanding of the work of the IMF throughout its membership, and supporting the Executive Board's institutional governance and oversight responsibilities.

The IEO's terms of reference provided for an external evaluation of the office, after an initial period, to assess its effectiveness and to consider possible improvements to its structure, mandate, operational responsibilities, or terms of reference. In the autumn of 2005, an independent panel of experts was appointed and, in April 2006 the Executive Board discussed their report.[1] The report assesses whether the IEO is meeting its goals to (a) serve as a means to enhance the learning culture within the IMF; (b) strengthen the IMF's external credibility; (c) promote greater understanding of the work of the IMF throughout its membership; and (d) support the Executive Board's institutional governance and oversight responsibilities. Section A discusses the work of the panel of experts as well as the Executive Board's reaction and follow up activities to the main findings and recommendations.

Key developments in FY2005–06, including outreach activities and relations with other evaluation offices are described in Section B, while Section C presents common messages that have arisen from evaluation reports. Appendix I describe procedures developed by the IEO that allow for extensive consultations in designing the evaluation project and also for receiving substantive inputs during implementation.

A. Evaluating the Evaluators: Messages from the External Evaluation of IEO

In April 2006, the IMF Executive Directors met to discuss the report prepared by an independent team of experts charged with evaluating the work of the IEO.[2] They agreed that the IEO had served the IMF well and earned strong support across a broad range of stakeholders. They also agreed that the IMF continued to need an independent evaluation office to contribute to the institution's learning culture and facilitate oversight and

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[1] The team consisted of Karin Lissakers, former U.S. Executive Director to the IMF (1993–2001), Dr. Ishrat Husain, Governor of the Central Bank of Pakistan, and Dr. Ngaire Woods, Director of the Global Economic Governance Program at Oxford University. The full terms of reference of the evaluation panel are given in Appendix V.

[2] The discussion is summarized in Public Information Notice No. 06/67; the report is available at *www.imf.org/external/np/pp/eng/2006/032906.pdf*.

governance by the Executive Board. In this connection, Directors welcomed the Panel's observation that the IEO has acted independently.

At the same time, Directors noted the weaknesses highlighted in the report and welcomed its analysis and recommendations for further strengthening the IEO's effectiveness. In particular, Directors concurred that a more focused and strategic orientation, together with strong support from the Board and management, would help ensure the IEO's continued usefulness and relevance.

To maintain the high quality of IEO reports, Directors call for them to be shorter, with more focused assessments and recommendations. Many Directors emphasized that the IEO should look beyond process to substance, including judgments on the theoretical foundations and analytical frameworks underlying the IMF's advice. Directors generally agreed with the Panel's recommendation that IEO outreach activities should be intensified.

Directors generally welcomed the Panel's suggestions for strengthening follow up to the IEO's recommendations—including more Board involvement. They considered that the Panel's call for a more systematic approach for following up on and monitoring the implementation of IEO recommendations approved by the Board should be further examined.

Directors were pleased that the IEO was taking the lead in reviewing its existing publications policy to ensure that it reflected evolving best practice. They agreed that any changes in the IEO's publications policy should be consistent with ensuring its independence.

Directors considered it appropriate to conduct another external evaluation of the IEO in five years.

IEO has begun work on several areas within its purview following the Executive Board's discussion. This includes a review of outreach and communication strategies, an analysis of human resource implications of the panel's recommendations, and updating of the IEO's publication policy. The Evaluation Committee of the Executive Board has also begun reflecting on other issues, including follow-up to IEO evaluations.

B. Developments in FY2005–06

Five evaluation reports were completed during the period FY2005–06: on IMF Technical Assistance; the IMF's Approach to Capital Account Liberalization; IMF Support to Jordan, 1980–2004; the Financial Sector Assessment Program (FSAP); and Multilateral Surveillance—see Table 1.1.[3] The main findings and lessons of these evaluations are discussed in Chapter II. An evaluation of IMF Structural Conditionality is nearing

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[3] The evaluation of IMF Technical Assistance was part of the Work Program of FY2004; the other four evaluations were in the Work Program of FY2005.

completion. Following the appointment of the new Director, the remainder of the work program for FY2006 was announced in June 2005.[4] That program included an evaluation of IMF advice on exchange rate policy; and on the IMF's role in selected African countries with respect to the external resource envelope, aid predictability and debt sustainability. A summary of ongoing projects is given in Chapter III.

The work program for FY2007, consisting of four projects to be added to the pipeline of future IEO evaluations, was decided after extensive consultation with a wide range of inside and outside stakeholders. The status of all completed and ongoing evaluation projects is given in Table 1.1.

Budget and staffing

The approved budget for FY2005 was $4.3 million. This amount includes staff costs, consultants, travel, outreach, and other miscellaneous costs (Appendix II).[5] As in previous years, a shortfall in actual expenditures occurred, largely reflecting delays in initiating some evaluation projects; actual expenditure was $3.7 million.[6] For FY2006, the approved budget was $4.46 million, representing a slight increase in real terms. The outcome is projected to be close to the approved budget. For 2007 the approved budget is $4.53 million, which implies a small decline in real terms.

The IEO's budget is equivalent to about 0.5 percent of the IMF's total administrative budget which is well below the average of over 1 percent that is spent on evaluation by other IFIs.

The IEO currently has 13 full-time staff positions, including the Director, the Deputy Director, 9 professionals, and 2 administrative assistants. The majority of the staff has been recruited from outside the IMF and has wide experience in relevant areas. Since the IEO's evaluation work is expected to involve constantly changing topics, there is a constantly evolving need for expertise of different types. This requires a greater use of consultants than in the IMF in general. The budget for consultants is about a quarter of the IEO's full-time staff budget.

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[4] See the Work Program for Fiscal Year 2006, available at http://www.imf.org/External/NP/ieo/2005/wp/eng/index.htm. The evaluation of structural conditionality, which is part of the FY2006 work program, had been announced earlier.

[5] The IMF's fiscal year begins May 1 and ends April 30.

[6] Excluding the costs of a consultant firm hired by the Executive Board to assist the search for a new Director, estimated at $96,000.

Table 1.1. Completed and Ongoing IEO Work Programs

Project	Status 2/
Initial round of evaluation projects	
Evaluation of Prolonged Use of IMF Resources	Completed (September 2002)
The IMF and Recent Capital Account Crises (Indonesia, Korea, Brazil)	Completed (May 2003)
Fiscal Adjustment in IMF-Supported Programs	Completed (August 2003)
FY2004	
The IMF and Argentina, 1991–2001	Completed (July 2004)
Evaluation of the IMF's Role in PRSPs and the PRGF	Completed (July 2004)
IMF Technical Assistance	Completed (January 2005)
FY2005	
The IMF's Approach to Capital Account Liberalization	Completed (April 2005)
IMF Support to Jordan	Completed (October 2005)
Financial Sector Assessment Program	Completed (November 2005)
Multilateral Surveillance	Completed (February 2006)
FY2006	
IMF Structural Conditionality	In progress (third quarter of 2006)
The Role of the IMF in the Determination of the External Resource Envelope in Sub-Saharan Africa	In progress (end-2006)
IMF Advice on Exchange Rate Policy	In progress (early 2007)
Latest additions to work program	
FY2007	
Aspects of IMF Corporate Governance—Including the Role of the Board	To commence
The IMF's Interactions with its Member Countries	To commence
The IMF's Research Agenda	To commence
The IMF's Approach to International Trade Issues	To commence

1/ Fiscal year reference indicates the year in which the projects were first added to the work program.

2/ The date refers to the time the completed report was, or is expected to be, circulated to the Evaluation Committee of the Board.

Outreach activities

One of the objectives of the IEO is to promote greater understanding of the work of the IMF. Accordingly, once an evaluation report is made public, the IEO engages in external outreach to make the evaluation report and the Board's decisions on it available to a wider audience. To promote this objective, various outreach events are organized to discuss each report after publication. To increase accessibility of the evaluation messages, a number of the country case studies have been translated into relevant local languages.[7]

[7] A full list of IEO publications is available on the IEO website at www.imf.org/external/np/ieo/pap.asp.

Between January 2005 and April 2006, the IEO participated in a number of outreach seminars and mid-pipeline workshops, often at the invitation of third-party organizers. These are listed in Appendix IV.

Relations with other evaluation offices

Since independent evaluation is now a feature of all IFIs and there are evaluation offices in all bilateral donor agencies, there are networks of such offices that exchange information on issues of mutual interest, including methodological approaches. The IEO is a member of the Evaluation Cooperation Group (ECG), which comprises the evaluation offices of multilateral development banks and the IMF and aims to strengthen the use of evaluation for greater effectiveness and accountability as well as to share lessons and harmonize approaches (www.ecgnet.org). The IEO also participates in the activities of the Development Assistance Committee Network on Development Evaluation, an international network of development evaluation experts and managers under the auspices of the Organization for Economic Cooperation and Development (OECD), which seeks to improve evaluation practice by sharing methods and experience and by elaborating technical guidance. Two IEO evaluations (of the Poverty Reduction Strategy Papers (PRSP)/Poverty Reduction and Growth Facility (PRGF) and of the FSAP) have involved reviews of activities where interaction between the IMF and World Bank was very close. In these cases, the World Bank's Independent Evaluation Group (IEG)[8] undertook parallel evaluations of World Bank activities and the two offices collaborated closely on the inputs, including through joint country case studies and joint surveys of various stakeholders.

Some common messages from IEO evaluations

Each of the two previous IEO Annual Reports highlighted a number of overarching themes that have emerged in many evaluation reports.[9] Some cross-cutting messages have arisen with striking regularity, including in the evaluations completed over the last year and a half. The prevalence of some common findings across a wide range of activities suggests that they reflect deep-seated attributes of the institution's culture and internal incentives that can be difficult to change. Indeed, the medium-term strategic review that is currently underway in the IMF is seeking to address many of the same issues.

While we will not repeat here the detailed discussion of previous Annual Reports, it is useful to reiterate three broad messages that have emerged in many evaluations.

The need for greater clarity about the goals of various initiatives, including criteria for judging how effective the IMF's own activities have been. Many evaluations, ranging

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[8] Previously the Operations Evaluation Department (OED).

[9] See Chapters 4 of the 2003 and 2004 Annual Reports, available at www.imf.org/ieo.

from the Prolonged Use of IMF Resources to the Evaluation of the IMF's Role in PRSP/PRGF and IMF Technical Assistance (TA), have flagged the lack of sufficiently clear goal posts for what the institution is trying to achieve with certain initiatives and the corresponding lack of performance indicators to track progress against those criteria. This lack of clarity can appear as excessive ambiguity about the concrete intermediate objectives of particular activities, with final objectives being so general that outcomes can never be attributed to the IMF even ex post (an issue flagged, for example, in the PRSP/PRGF evaluation report where measuring rods for what the IMF, as an institution, is expected to achieve in the PRSP process are too vague) or as too long a list of "priorities" that make it difficult to make tradeoffs and blur accountability when it is time to assess results (a finding of the TA evaluation report). The recently completed FSAP evaluation, discussed in the next chapter, highlights a similar potential issue with regard to priority setting, in this case arising from the emphasis on both stability and development aspects of the financial sector and the joint IMF-world Bank nature of the initiative. The evaluation of the IMF's Approach to Capital Account Liberalization, also discussed in Chapter 2, indicates that there is ambiguity about what concretely is expected of the IMF in this area and that the Executive Board could usefully clarify the place of capital account issues in IMF surveillance.

Setting concrete intermediate objectives, which can then be monitored to assess effectiveness and determine priorities, is a challenge for any organization. Two aspects of the channels through which the IMF influences its ultimate objectives make the challenge especially complex. First, the ultimate objectives (e.g., faster growth or poverty reduction) are at the end of a long, complex results chain, so "attribution" of final outcomes to IMF activities is generally not possible. For example, most channels of IMF influence operate through effects on policy decisions in individual member countries that are inevitably difficult to calibrate. This complicates the setting of monitorable intermediate objectives for surveillance activities in particular.[10] Second, many key intermediate outcomes of interest to the IMF—reduced vulnerability to external crises, financial system stability, etc.—can only be defined in probabilistic terms. For example, the FSAP evaluation report notes that a key objective of the FSAP exercise—financial system stability—is not defined in any of the policy papers establishing the initiative. But these aspects should not prevent the IMF from setting clearer priorities about what it will deliver and establishing benchmarks to monitor progress. For instance, the FSAP evaluation notes that, in deciding and monitoring priorities for coverage of financial sector surveillance, the extent and frequency of FSAPs and FSAP Updates for countries of global or regional systemic importance would be one useful benchmark.

The IMF should lay out its "intellectual capital" by explaining better the rationale for policy advice and program design in particular countries. The fiscal and PRSP/PRGF

[10] Some of these issues are discussed in "Strategy Design in Evaluating IMF Surveillance Activity,"IEO Background Paper prepared by Paul Duignan and Nils Bjorksten, also available at http://www.imf.org/External/NP/ieo/2005/bckgn/BP051.pdf.

evaluations both noted that many IMF program documents contain little explanation of the underlying rationale for key program assumptions (e.g., on the magnitude of the targeted adjustment in fiscal deficits), which makes it difficult for outsiders to judge the reasonableness of program design. The recent Jordan evaluation reinforces this finding. The evaluations suggest that greater openness about the rationale for particular aspects of program design can contribute to better outcomes—by widening the "policy space" of potential choices that are considered and by clarifying the basis for any subsequent program modifications, should actual outcomes deviate from program assumptions. The experience with the 2000 PRGF-supported program for Tanzania, discussed in the PRSP/PRGF evaluation, gives one example of how broadening the debate to include inputs from other groups had a beneficial effect on program design. The initial program assumed a more rapid "crowding in of the private sector" than occurred in practice and also proved to be too pessimistic about available aid inflows, but the IMF did show flexibility in adapting the program to revised circumstances—assisted by donor-funded studies by outside academic advisors that provided important inputs into the design.[11]

The need for greater candor in papers submitted to the IMF Board is a message common to almost all IEO evaluations. Candid assessments are especially needed to improve the effectiveness of surveillance (an important finding of the evaluations of the Role of the IMF in Recent Capital Account Crises, the IMF Role in Argentina and, most recently, in the FSAP evaluation—where the evidence suggests a "loss in translation" between vulnerabilities identified in FSAP reports and the associated IMF surveillance). The Jordan evaluation also reiterates the message of earlier evaluations (e.g., of Prolonged Use of IMF Resources, and the Role of Fiscal Adjustment in IMF-Supported Programs) that papers submitted to the Board on IMF-supported programs often downplay potential risks. All these evaluations suggest that while a vigorous internal debate on key risks and potential tradeoffs may take place within the IMF staff, the presentation to the Board is often much more muted. There are deep-seated sets of incentives that produce this outcome: (i) area departments are directly responsible for the content of country reports and are most concerned with maintaining a harmonious country relationship; (ii) as noted, assessments of potential vulnerabilities essentially involve judgments on probabilities, on which reasonable people can differ and where there is a natural—and appropriate—tendency to give member countries the "benefit of the doubt," and (iii) especially in program cases, staff is concerned to maximize the chances of a program's success, which often leads to potential risks not been highlighted. In many cases—perhaps illustrated most sharply in the Argentina evaluation (e.g., the sustainability of the exchange rate)—concerns that sensitive and potentially damaging analysis could leak caused issues not to be addressed in Board papers. While understandable, all of these factors lead to a weakening of the oversight role of the Board.

[11] See "Box 4.2. Tanzania: Alignment, Fiscal Flexibility, and Program Design" of the *Evaluation of the IMF's Role in the PRSP and PRGF*, available at http://www.imf.org/External/NP/ieo/2004/prspprgf/eng/index.htm.

II. Evaluation Projects Undertaken in FY2005–06

This chapter summarizes the main findings and recommendations of the five most recently completed evaluation reports along with the conclusions reached in the respective Executive Board discussions.

A. IMF Technical Assistance

This evaluation examines the technical assistance (TA) provided by the IMF to its member countries. It is based on desk reviews of a sample of countries, cross-country data on TA, six in-depth country case studies[12] (including field visits and interviews with public officials and donors, reviews of past evaluations, and interviews with IMF staff and other stakeholders).

To derive operational lessons, the evaluation unbundles TA into the following three stages:

- **Prioritization**: How are countries' TA needs identified? What can be done to make the process more strategic so as to increase the relevance of IMF TA activities?

- **The delivery process**: What factors influence the effectiveness of the various modalities for TA delivery?

- **Monitoring progress and evaluating impact**: How is progress tracked and what factors contribute to the impact of TA?

Main findings

How are TA priorities set?

- The IMF provides annually about 300 person-years of direct TA, amounting to about 10 percent of the gross administrative budget of the institution. Seventy percent of TA is directed to countries with per capita income below $1,000, thus IMF TA is well targeted to low-income countries. The volume of TA provided to countries is also positively associated with having a PRGF- or EFF-supported program, the amount of external financing available, and whether the country is emerging from conflict.

- There is a weak link between TA priorities and PRSPs or with key policy issues identified in Article IV consultations. In most cases, the PRS process has not yet been able to clearly identify major capacity-building needs to be taken up by TA. This is a major shortcoming because the PRSP was expected to provide guidance on broad priorities for the IMF in low-income countries. As a result, TA activities do not appear to be guided by a medium-term country-based policy framework that would

[12] Cambodia, Honduras, Niger, Ukraine, Yemen, and Zambia.

set priorities in the IMF areas of expertise *across* sectors, program needs, and institutional initiatives, and that would *balance* TA demands stemming from short-term policy needs with medium-term capacity-building needs.

The process of TA delivery

- Country officials have generally been satisfied with the resident experts provided by the IMF, particularly their hands-on role in training and coaching, accessibility, and emphasis on teamwork. However, the evaluation finds that the involvement of the authorities in the preparation of terms of reference (TOR), especially for long-term experts, is generally passive. This tends to reduce ownership and mask important differences in expectations between the authorities and staff about final objectives.

- Country officials noted that more informal and iterative discussions on a broader set of options before the wrap-up meetings at the end of a TA mission would contribute to enhancing ownership of recommendations by ensuring that constraints on the ground are taken into account.

- The evaluation found many instances of weak coordination between the IMF and donors working in similar areas. While coordination with donors is, in principle, the authorities' responsibility, in practice this is rarely the case owing to weak institutional capacity and the fact that the PRSP is not yet sufficiently operational to play such a role in most low-income countries. As a result, the burden of coordinating donors' efforts often falls to a major donor or multilateral institution. Moreover, when the involvement of donors is strong in a particular country, and the IMF provides a relatively small fraction of TA, it is not always possible or even appropriate for the IMF to provide leadership in coordinating overall TA efforts even in its core areas of expertise. However, it should still seek to coordinate better with donors working in similar areas and, in low-income countries, should help governments make the PRS an effective vehicle on which it can align its own efforts.

Monitoring the impact of TA and evaluating factors influencing it

- The case studies show that progress has generally been achieved in enhancing the technical capacity of the agencies that the IMF typically supports. Significant variability was found, however, on whether agencies have been able to make full use of the increased capacity in order to have an impact on the ground or in achieving the ultimate objectives of TA. It is critical that the IMF understands fully what prevents agencies from doing so.

- Part of the problem is that IMF documentation and reporting does not clearly unbundle and track the different stages of progress toward meeting the final objectives of TA. Specifically, documentation is weak in:

- defining at the outset indicators (benchmarks) to judge whether progress is occurring, and explicitly discussing these indicators with the authorities;

- unbundling between short- and medium-term indicators that capture different stages of the results chain, for example, (a) indicators that track the improved technical abilities of agencies receiving TA; (b) indicators that show whether these agencies are actually using that increased know-how, for example, whether they are performing their responsibilities; and (c) indicators that track the economic outcomes of that enforcement.

- The absence of a clear unbundling of these stages, and the factors influencing the lack of progress, limits the ability to use track record in implementing TA in making decisions about future TA. This is critical because there may be good reasons why TA recommendations have not been implemented.

- Frequently political interference or lack of support by the authorities prevent agencies from using effectively the knowledge transmitted by TA. Indeed, the case studies suggest that resistance by vested interests may mount as these agencies improve their ability to act. The evaluation found that in these cases the reporting from the field on constraints to progress has often not been sufficiently candid so that the ways to address such obstacles were generally not discussed frankly with the authorities.

Main recommendations

The main recommendations of the evaluation are as follows:

Recommendation 1. The IMF should develop a medium-term country policy framework for setting TA priorities, incorporating country-specific strategic directions and linked to more systematic assessments of factors underlying past performance.

- In low-income countries, the PRS process provides the natural framework to identify TA capacity-building priorities, although it has infrequently been used effectively for this purpose. The IMF needs to engage countries to help them articulate their medium-term capacity-building needs in the IMF's areas of responsibility and in accordance with the PRSP. For other countries where there is a relatively significant provision of IMF TA, the framework may require periodic in-depth consultations with the authorities comprising an analysis of past progress and a forward-looking exercise to identify priorities.

- Area departments and resident representatives could play a greater role in developing these frameworks and this role should be explicitly acknowledged.

Recommendation 2. The IMF should develop more systematic approaches to track progress on major TA activities and to identify reasons behind shortfalls.

- At the outset of major TA activities, IMF staff and the authorities should agree on how the success of the TA activity will be measured. The IMF staff should unbundle more clearly the different stages through which TA has an impact, and then monitor these stages. Specifically, it should differentiate between:

    - progress in improving the technical capacities of agencies receiving TA;

    - whether agencies are making effective use of that increased technical capacity; as well as reasons on why this is not happening; and

    - the impact on the ground in terms of economic outcomes.

- Resident experts and headquarters' staff in charge of backstopping activities should be candid in reporting obstacles to progress, including political interference or lack of support from the authorities, that prevent agencies from making effective use of their improved technical capacity.

Recommendation 3. Greater involvement by the authorities and counterparts in the design of TA activities and arrangements for follow-up should be emphasized as a signal of ownership and commitment

- IMF staff should request the authorities and specialized counterparts to fully participate in the preparation of the TOR and devote sufficient time to help design the activity. Willingness to do so should be one of the factors taken into account in decisions on TA resource allocation.

- For more complex multiyear TA activities, a letter of agreement between the authorities and the IMF could specify commitment and resources including (a) mutually agreed benchmarks of progress, (b) commitments by both the IMF and the authorities—to assure sustainability beyond the life of the TA activity; and (c) critical policy steps that are required from the authorities to ensure necessary institutional changes, such as decrees or legislation that complement the TA activity.

- Greater efforts need to be made to disseminate the lessons of specific TA activities within relevant government departments and agencies.

Recommendation 4. Stronger efforts should be made by TA experts to identify options and discuss alternatives with local officials prior to drafting TA recommendations

- The receptivity of TA recommendations seems to be enhanced greatly when IMF experts engage counterparts early on in the design of the activity, explain its motivation, and try to assess the institutional subtleties of the specific environment. There is also a need to allow enough time for informal discussions prior to issuing recommendations and the wider consideration of options. TA missions should allow enough time to incorporate these factors even if the result is somewhat longer missions and correspondingly fewer TA activities.

Recommendation 5. To more effectively guide TA allocation, some strategic decisions on trade-offs need to be taken

- An effective priority-setting process needs two components: (i) strategic direction by the Executive Board and management in areas where the IMF will seek to maintain or develop "core competencies;" and (ii) an internal system that allocates resources effectively among competing demands, guided by these strategic objectives.

- Different approaches to balancing these two components are possible—essentially involving a decision on how decentralized the process should be. The advantage of a more decentralized approach is that TA can be closely aligned with specific country needs which is important given the large variation in country circumstances within the IMF membership. However, given that the TA resources of the IMF are small relative to global efforts, such approach has the risk of spreading the expertise of the IMF too thinly. Providing sharper strategic directions may help build a critical mass of expertise, but it may do so at the expense of adaptability to country circumstances. These are the key trade-offs that should be decided as part of an overall TA strategy.

Executive Board response

The Executive Board discussed the report on February 2005. The Board welcomed the report and its recommendations.

Improved prioritization

- Most Directors agreed that in low-income countries the PRSP should increasingly serve as a vehicle for identifying medium-term TA needs and improving coordination of TA among various agencies. In other countries, Directors stressed the importance of developing country-centered frameworks for identifying TA needs, but noted that a variety of approaches—possibly including greater use of Article IV consultations to assess needs—may be appropriate.

- Directors saw value in the annual resource allocation plan (RAP) evolving toward a multiyear framework, with area departments taking a central role in developing country frameworks, and resident representatives, where present, also contributing to identifying and monitoring TA. This approach would allow a comprehensive comparison across sectors and countries between TA needs—as prioritized by the area departments. It would also provide means of identifying emerging pressure points that might call for a reallocation of resources across TA-providing departments. Directors emphasized that a multiyear framework should retain the flexibility to satisfy unexpected TA needs where appropriate.

Tracking and monitoring

- Directors supported the recommendation that at the outset of major TA activities, staff and the authorities should agree on measurable indicators of progress covering all the major stages of the activity. Directors saw a need for better tracking progress by unbundling the different stages of the TA project life cycle, careful explanation of the shortfalls in project execution, and candid reporting by staff of obstacles to progress. A number of directors cautioned against using tracking indicators mechanistically for making decisions on future TA allocations.

Greater involvement of local authorities and experts

- Directors concurred that greater involvement and ownership by the recipient authorities and discussion of options are crucial to greater TA effectiveness. They welcomed the proposals for more participation by country authorities in drawing up TOR building on the discussions that already take place. This will require systematic dialogue by all parties to specify clearly progress milestones, resource commitments, and critical policy steps required for the final success of TA.

Guiding TA overall resource allocation

- Directors considered that prioritization of TA resources should flow from a shared vision of the IMF's overall medium-term objectives—reflecting its core competencies—while at the same time retaining the flexibility to respond to the urgent needs of members. An approach led by area departments could allow TA to be closely aligned with specific country needs and circumstances and better integrated into the IMF's surveillance, and program activities. At the same time, however, the discussion also highlighted that this approach might risk spreading expertise too thinly. Several Directors stressed that some centralized guidance on broad policy priorities for IMF TA could help build a critical mass of expertise, but recognized that this could be at the expense of adaptability to country circumstances. In this context, some concern was expressed over the volume of TA that is being driven by IMF-wide initiatives.

- Directors also noted that the IEO report raises a range of broad issues which they looked forward to discussing in the context of the ongoing strategic review of the IMF.

B. The IMF's Approach to Capital Account Liberalization

The role of the IMF in capital account liberalization has been a topic of controversy, against the background of highly volatile international capital flows and the associated financial instability experienced by a number of major emerging market economies in recent years. The IMF's role is particularly controversial because capital account liberalization is an area where there is little professional consensus. Moreover, although *current account liberalization* is among the IMF's official purposes outlined in its Articles of Agreement, the IMF has no explicit mandate to promote *capital account liberalization*. Nevertheless, the IMF has given greater attention to capital account issues in recent decades, in light of the increasing importance of international capital flows for member countries' macroeconomic management.

The evaluation report reviews the IMF's policy advice on capital account liberalization and related issues in a sample of emerging market economies over the period 1990–2004. It seeks to (i) contribute to transparency by documenting what in practice has been the IMF's approach to capital account liberalization and related issues; and (ii) identify areas, if any, where the IMF's instruments and operating methods might be improved, in order to deal with capital account issues more effectively. The issues addressed in the evaluation cover not only capital account liberalization but also capital flow management issues, including particularly the temporary use of capital controls. However, the evaluation does not address the question of whether liberal capital accounts are intrinsically beneficial—on which the broader academic literature has not been able to provide a definitive answer—or whether the Articles of Agreement should be amended to give the IMF an explicit mandate and jurisdiction on capital account issues. Many aspects of these issues are not amenable to evidence from the evaluation. However, the evaluation does shed some light on the consequence of the lack of explicit mandate and jurisdiction on the IMF's work on capital account issues.

The report begins by reviewing the IMF's general operational approach and analysis as they evolved from the early 1990s into the early 2000s. It then assesses the IMF's country work in terms of (i) its role in capital account liberalization during 1990–2002; (ii) its policy advice to member countries on managing capital flows during the same period; and (iii) its ongoing work on capital account issues (where outstanding issues are identified for 2003–04). The report concludes by offering two broad recommendations.

Major findings

The evaluation finds that the IMF encouraged countries that wanted to move ahead with capital account liberalization, especially before the East Asian crisis. However, there is no evidence to suggest that it exerted significant leverage to push countries to move faster than they were willing to go. The process of liberalization was often driven by the authorities' own economic and political agendas, including OECD or EU accession and commitments under bilateral or regional trade agreements. In encouraging capital account liberalization, the IMF pointed out the risks inherent in an open capital account as well as the need for a sound financial system, even from the beginning. These risks, however, were insufficiently highlighted, and the recognition of the risks and preconditions did not translate into operational advice on pace and sequencing until later in the 1990s.

In multilateral surveillance, the IMF's analysis emphasized the benefits to developing countries of greater access to international capital flows, while paying comparatively less attention to the risks inherent in their volatility. As a consequence, its policy advice was directed more towards emerging market recipients of capital flows, and focused on how to manage large capital inflows and boom-and-bust cycles; little policy advice was offered on how source countries might help to reduce the volatility of capital flows on the supply side. In more recent years, the IMF's analysis of such supply-side factors has intensified. Even so, the focus of policy advice—beyond the analysis of macroeconomic policies covering large current account imbalances—remains on the recipient countries.

In country work there was apparent inconsistency in the IMF's advice on capital account issues. Sequencing was mentioned in some countries but not in others; advice on managing capital inflows was in line with standard policy prescriptions, but the intensity differed across countries or across time; and a range of views was expressed on use of capital controls (though greater convergence toward accommodation of such controls was observed over time). Policy advice must of necessity be tailored to country-specific circumstances, so uniformity cannot be the only criterion for judging the quality of the IMF's advice. Country documents, however, provide an insufficient analytical basis for making a definitive judgment on how the staff's policy advice was linked to its assessment of the macroeconomic and institutional environments in which it was given. Even so, it appears that the apparent inconsistency to a large extent reflected reliance on the discretionary judgments of individual IMF staff members.

The evaluation suggests that the IMF has learned over time, and some of the learning became more quickly reflected in the IMF's country work through its impact on individual staff members. The lack of a formal IMF position on capital account liberalization gave individual staff members freedom to use their own professional and intellectual judgment in dealing with specific country issues. In more recent years, somewhat greater consistency and clarity has been brought to bear on the IMF's approach to capital account issues. For the most part, the new "integrated" approach upholds the role of country ownership in determining pace and sequencing; takes a more consistently cautious and nuanced position towards encouraging capital account convertibility; and acknowledges the usefulness of capital controls under certain conditions. However, because the approach identifies a complex set of risks without offering clear criteria for balancing those risks, it has proven to be difficult to apply in practice. There continues to be some uneasiness on the part of some staff with the lack of a clear position by the institution.

Recommendations

The evaluation suggests two main areas in which the IMF can improve its work on capital account issues.

Recommendation 1. There is a need for more clarity on the IMF's approach to capital account issues. The evaluation is not focused on the arguments for and against amending the Articles of Agreement, but it does suggest that the ambiguity about the role of the IMF with regard to capital account issues has led to some lack of consistency in the work of the IMF across countries. With or without a change in the Articles it should be possible to improve the consistency of the IMF's country work in other ways. Possible steps could include the following (although other approaches are also possible and the specifics would be for the Board to decide):

- The place of capital account issues in IMF surveillance could be clarified. It is generally understood that the IMF has a responsibility to exercise surveillance over certain aspects of members' capital account policies, to the extent that capital account policy is intimately connected with exchange rate policy. There would be value if the Executive Board were formally to clarify the scope of IMF surveillance on capital account issues.

- The IMF could sharpen its advice on capital account issues, based on solid analysis of the particular situation and risks facing specific countries. Given the limited consensus in the literature, the IMF's approach to any capital account issue must necessarily be based on an analysis of each case. To assist the authorities in deciding when and how to open the capital account, the IMF should provide an operationally meaningful indication of the benefits, costs, and risks (and, indeed, practicality) of moving at different speeds.

- The Executive Board could issue a statement clarifying the common elements of agreement on capital account liberalization. There remains considerable uncertainty among many staff members on what policy advice to provide to individual countries. This has led to hesitancy on the part of some within the staff to raise capital account issues with country authorities. The Executive Board could provide clear guidance to staff on what the IMF's official position is.

Recommendation 2. The IMF's analysis and surveillance should give greater attention to the supply-side factors of international capital flows and what can be done to minimize the volatility of capital movements. The IMF's policy advice on managing capital flows has so far focused to a considerable extent on what recipient countries should do. Building on recent initiatives, the IMF should also provide analysis of what can be done to minimize the volatility of capital flows by operating on the supply side. However, as was clarified during the Board discussion, the intention of this recommendation is not to suggest that the IMF should become heavily involved in detailed regulatory matters.

Executive Board response

The Executive Board discussed the report on May 11, 2005. The Board welcomed the report and broadly endorsed the thrust of its findings, though it expressed a range of views on the recommendations. Directors noted that the report offered a broadly accurate account of the evolution of IMF thinking and practice on capital account issues, and welcomed the IEO's confirmation that the IMF did not apply an inappropriate "one-size-fits-all" approach to capital account liberalization. They considered that the IMF should continue to adopt a flexible approach to capital account liberalization that takes due account of countries' specific circumstances and preferences.

The Executive Board's responses to specific recommendations are summarized below.

The place of capital account issues in IMF surveillance could be clarified.

Directors stressed that the IMF has long attached importance to capital account issues and vulnerabilities, and that the process of clarifying their role in surveillance is well under way. They noted that the Executive Board, in its various discussions, has called for IMF surveillance to adjust to the changing global environment, notably the expansion in capital flows. Some Directors, however, saw merit in further clarifying the scope of IMF surveillance to recognize explicitly the central importance of capital account policies. On the broader aspects of the IMF's role in capital account liberalization, most Directors did not wish to explore further at present the possibility of giving the IMF jurisdiction over capital movements.

The IMF could sharpen its advice on capital account issues.

Directors agreed that the IMF has an inherent responsibility to its members to analyze the benefits and risks involved in a world of open capital markets, and to provide practical, sound, and appropriate policy advice to its members on those issues. With regard to the IEO's suggestion that the IMF staff should aim to provide more quantitative assessments of the benefits, costs, and risks of liberalizing the capital account at different speeds, a few Directors saw merit in the proposal, while others considered it to be very difficult to implement because of the technical challenges and economic complexities involved.

The Executive Board could issue a statement clarifying the common elements of agreement on capital account liberalization.

Directors expressed a variety of views on the merit of an Executive Board statement clarifying the elements of agreement on capital account issues. A number of Directors supported such a statement, which could build on the "integrated" approach that has gradually evolved in the IMF's operational work. However, many Directors underlined the challenge that would be faced in developing such a statement in view of the inherent difficulty in developing common guidelines that adequately take into account country-specific circumstances, particularly given the lack of firm theoretical and empirical conclusions. Directors stressed that staff will need to continue to exercise their informed professional judgment and discretion.

The IMF's analysis and surveillance should give greater attention to the supply-side factors of international capital flows and to what can be done to minimize the volatility of capital movements.

Directors welcomed the various initiatives under way in the IMF to strengthen research, analysis, and surveillance of the supply side of capital flows, and agreed with the IEO's view that considerable progress has already been made in this area. Directors encouraged the staff to continue to build on the work already being undertaken to further its understanding of supply-side factors and their operational and policy implications. Directors cautioned that any expanded work should not entail IMF involvement in the regulation of the sources of capital, noting that the IMF should instead coordinate with those who have the necessary expertise and mandate in the setting of standards.

In concluding, Directors agreed that the IMF's future work on capital account issues should seek to buttress efforts to promote financial stability, while helping ensure that controls are not used as a substitute for adjustment. This strategy would imply orderly and non-discriminatory liberalization aimed at facilitating countries' integration into the global economy while maintaining stability. As a follow up to the findings of the IEO report, Directors looked forward to capital account issues being addressed in the context of the IMF's ongoing strategic review.

C. IMF Support to Jordan, 1989–2004

The evaluation report examined the extent to which the IMF contributed to tackling Jordan's major macroeconomic challenges during the extended period (1989–2004) of the country's engagement in IMF-supported programs.[13] Although the main focus of the evaluation was on the effectiveness of the IMF-supported programs, the roles of IMF surveillance and technical assistance activities were also examined. The Jordan case study provided an opportunity to revisit—in a specific country context—previous IEO findings and lessons on issues related to: (i) program design; (ii) interactions between programs, surveillance and technical assistance activities; and (iii) the impact of prolonged engagement in IMF-supported programs on the development of domestic institutions and policy making processes.

[13] The programs were supported under three Stand-By Arrangements (approved in 1989, 1992, and 2002) and three Extended IMF Facility arrangements (approved in 1994, 1996, and 1999).

Overview

At the start of its long period of participation in IMF-supported programs in the late 1980s, Jordan faced a severe balance of payments crisis as well as deep-rooted macroeconomic and related structural problems. It faced a massive external public debt, and large deficits in the external current account and government budget. A rigid fiscal structure and structural impediments to growth meant that sustainable adjustment was going to be hard to achieve, and would require time to be addressed effectively. In addition, Jordan's close regional economic ties made it susceptible to shocks related to economic and political developments in the Middle East.

The report's overall assessment of the IMF's role in Jordan is that it was moderately successful. The IMF helped the authorities to address macroeconomic stabilization challenges successfully, but some of the main structural rigidities that underlay the financial crisis still remained, especially on the fiscal side. As in all programs which are the outcome of a complex negotiating process, the IMF was required to make judgments reflecting considerations of domestic ownership and political feasibility. The result was inevitably tempered by this reality.

Main findings

Appropriateness of program design

Program objectives were relevant to Jordan's circumstances, and were consistent with broad objectives spelt out in the authorities' national development plans. The programs supported under the early arrangements approached issues of external and fiscal sustainability primarily in flow, not stock, terms, reflecting the general status of international approaches to official debt relief at the time. Later programs did incorporate a more comprehensive approach to analyzing debt sustainability, in line with institution-wide developments.

Most Board papers on Jordan did not provide a clear rationale for the magnitude and composition of targeted adjustment, although there was some improvement in recent years. This made it difficult to make judgments on the factors underlying any subsequent failures to achieve key objectives, and on the appropriateness of any program modifications. Moreover, analysis of the links between growth objectives and program design was generally limited.

In general, structural conditionality was reasonably well designed and seems to have observed a clear division of labor with the World Bank. The main exception was the 1999 EFF where the IMF adopted a number of detailed benchmarks on privatization that were not well designed. Many senior Jordanian officials credited IMF conditionality with helping to implement politically sensitive reforms (e.g., introduction of the GST, rationalization of subsidies, and pension reforms), but also cited examples in which pressure from the IMF for speedy action backfired (e.g., submission of a draft income tax law to parliament with little prior consultation with members of parliament).

Macroeconomic outcomes and the role of IMF support

While attribution of specific final outcomes to IMF involvement is not possible, the report's overall judgment is that IMF-supported programs did make an important contribution. This view was shared by many Jordanian officials, past and present, who indicated that the presence of the IMF was important in reinforcing necessary macroeconomic discipline and in helping advance some key reforms.

However, fiscal sustainability was only partly achieved. While total and external public debt ratios fell substantially, only some of the underlying fiscal rigidities were resolved. Specific areas of success included the introduction of broader-based consumption taxation, the replacement of food price subsidies by targeted cash transfers, and reforms in the pension system; most of the latter reforms only took place late in the period of IMF program involvement and should have received greater emphasis earlier. Less successful were the following areas:

- Direct taxes still had significant levels of exemptions that erode potential revenue.
- Jordan had still not adopted a system of pricing for domestic petroleum with an automatic link to world prices—in spite of significant policy dialogue and TA on the part of the IMF.
- In spite of IMF documents constantly reminding readers about the inflexibility of public expenditures, little progress was achieved in these areas. The IMF did not put sufficient emphasis at an early stage of its program involvement on efforts at civil service reform.

IMF support and domestic institution building

In retrospect, the IMF could have taken a longer-term perspective from early on in its program involvement and could have started earlier to help the authorities put in place the necessary policies and institutions to achieve fundamental expenditure reforms. Later programs began to address some, but not all, of these rigidities. But shortcomings in reforms, like successes, cannot be attributed only to the IMF. As some of the above examples indicate, the authorities were not able to act on a number of rigidities even when the IMF did clearly diagnose the problem and suggest possible courses of action.

The report found that IMF TA priorities adapted quite well to Jordan's critical needs—with an increased involvement of the authorities in setting such priorities. However, a greater focus on public expenditure policy to advise on the major expenditure cuts envisaged in the early programs would have been desirable. IMF-World Bank cooperation in this area was not effective (see below). Based on an examination of policy implementation as well as interviews with authorities and experts in the field, the report concludes that IMF TA made a substantial and contribution in the areas of tax policy and administration, rationalization of food subsidies, public financial management, pension reforms, monetary operations, payment systems and banking supervision.

The report found little awareness of the contribution of IMF TA and the associated policy dialogue outside recipient agencies. A wider dissemination of IMF TA reports would have contributed to more informed public discourse on a number of policy issues.

IMF internal processes and policies

Coordination between the IMF and World Bank staffs was effective in many areas, with a clear division of labor between the two from an early stage. However, in the key area of public expenditure policy, collaboration was not effective; in particular, the World Bank's public expenditure reviews provided limited input to the fiscal policy content of IMF-supported programs.

The report found no significant evidence that Jordan enjoyed preferential treatment from the IMF in terms of access to IMF resources, programmed levels of fiscal adjustment or the provision of TA.

Lessons from Jordan's experience

Broad lessons suggested by the IMF experience in Jordan

Lesson 1. The Jordan case reinforces the view that the underlying rationale for key program design elements should be explained clearly in Board papers. In particular, judgments on the magnitude and composition of targeted adjustment need to be grounded in an explicit assessment of external and public debt sustainability over the medium term.

Lesson 2. Internal notes by staff tended to be franker than reports prepared for the Executive Board about the risks to Jordan's programs. For example, the treatment of the upsurge in grants during 2003–04 said relatively little about the risk of a sharp reversal and the challenges of managing such a reversal. This illustrates the need for more candor in staff report assessments of risks to programs.

Lesson 3. Jordan's experience suggests that the nature of short-term fiscal conditionality alone—i.e., whether to set performance criteria on the fiscal deficit before or after grants—can be of only limited help in dealing with the underlying issue of large and abrupt surges in grants. Such situations require that programs be set in an explicitly longer-term perspective that take account of the likely duration of the upturn in grants.

Lesson 4. The IMF's program involvement in Jordan would have been more effective if programs had given greater emphasis at an earlier stage to the formulation of key institutional reforms in the fiscal area even if, as was likely, they could not be fully implemented during the initial program period.

Lesson 5. While the reasons why World Bank inputs on public expenditure policy and management could not be incorporated into IMF program design were probably specific to Jordan, the lesson of more general applicability is that the two institutions need to set clear objectives for such integration to be achieved, including through signaling what the needs and obligations of each institution are, along with candid and timely reporting to the Board on any emerging problems in meeting these priorities.

Lesson 6. Jordan's experience suggests that, at least in certain circumstances, structural conditionality can have significant value added in terms of encouraging and monitoring progress on reforms. However, unrealistically "tight" deadlines can be counterproductive. Timetables need to be designed carefully, taking account of the political economy situation, especially when legislative action is involved.

Lesson 7. A wider dissemination of IMF TA reports would have contributed to more informed public discourse and shed light on the rationale for IMF policy advice on key issues.

The IMF's future role in Jordan

Lesson 8. Looking ahead, the IMF's main challenge will be to help Jordan manage the projected decline in grants in a manner that preserves the gains made in the areas of macroeconomic stability and longer-term fiscal sustainability. This suggests that the highest priorities for policy advice and technical assistance should be on helping the authorities design a macroeconomic framework—and an explicit delineation of accompanying policies—that will achieve a smooth transition.

Lesson 9. An important part of IMF assistance should focus on helping to design strategies to tackle Jordan's key remaining fiscal rigidities. The focus should be on exploring alternative policy options to achieve the necessary structural reforms in the fiscal area. Previous experience suggests that short-term quantitative targets without analyzing in greater depth the underlying strategies to achieve these targets are unlikely to be successful.

Executive Board response[14]

The Executive Board discussed the report on November 21, 2005. The discussion focused on the following issues:

Successful macroeconomic stabilization. Directors agreed with the report's overall assessment that Jordan's long engagement in IMF-supported programs had helped the

[14] The full Summing Up of the Executive Board discussion is available on the IEO website at www.imf.org/External/NP/ieo/2005/jor/eng/index.htm. Staff and management responses to the evaluation report are also available at the website.

authorities address macroeconomic stabilization challenges successfully, although some of the main structural rigidities that underlay the financial crisis that led Jordan to its first IMF-supported program still remain to be addressed.

Foreign grants and fiscal rigidities. The Board shared the view that Jordan still faces the challenges of adjusting to a sharply lower level of foreign grants and reducing fiscal rigidities. Most Directors noted that these challenges would have been less daunting had more progress been made on critical reforms during Jordan's longer-term program engagement, including an increase in the flexibility of public expenditure and introduction of an automatic formula to allow domestic fuel prices to reflect world oil prices. They considered that a longer-term perspective, with greater emphasis at an earlier stage on the formulation of key institutional reforms in the fiscal area, would have increased the effectiveness of IMF-supported programs in Jordan, even if the reforms were to be completed only at a later stage.

Exchange rate policy. Directors took note of the evolution of the IMF's advice on exchange rate policy, while recognizing that the peg has generally served Jordan well during the period under review. Many Directors shared the perception that the advice to Jordan for a shift to a more flexible exchange rate regime has been more a reflection of the evolution of the IMF's view on exchange rate policy in general rather than based on Jordan's circumstances. They felt that the staff's advice could have taken more fully into account Jordan's specific susceptibility to real and nominal shocks, as well as its vulnerabilities. Many other Directors observed, however, that the increasing emphasis on the merits of a flexible exchange rate regime in the later part of its longer-term program engagement had been appropriate in light of the increasing importance of real and external shocks. In any event, Directors continued to see a need for candor in the treatment of exchange rate policy in Board documents.

Dissemination of IMF TA reports. Directors concurred with the IEO's lesson that a wider dissemination of IMF TA reports could have contributed to more informed public discourse and shed light on the IMF policy advice on key issues. At the same time, Directors noted that decisions on disseminating such reports are ones for the authorities to take. A number of Directors observed that, in some cases, wider dissemination of TA reports could also increase resistance to reforms, particularly by creating the perception about policy changes being externally imposed. They considered that the country authorities are best placed to determine whether increased awareness of TA reports would help in reform implementation.

Internal processes and policies and coverage of the IEO report. The Board welcomed the IEO's analysis of issues related to the IMF's internal processes and policies. They noted that the analysis found no significant evidence that the nature of Jordan's longer-term program engagement reflects preferential treatment because of this member's geopolitical position. A number of Directors, however, felt that the IEO report could have explored more deeply the nature of IMF decision-making in the case of Jordan.

Rationale for key elements of program design. Many Directors agreed that the Jordanian experience reinforces the need for Board papers to provide clearly the underlying rationale for key elements of program design. They also supported the IEO's call for greater candor in staff report assessments, especially of the risks to the program and recommendations on how best to mitigate and manage them. These steps were seen as ensuring accountability by staff and management, and enabling the Board to take more informed decisions and to exercise its oversight responsibilities more effectively. While agreeing that structural conditionality had been well designed, many Directors also pointed to the lessons for the timing of these conditions offered by the Jordanian experience. In particular, they noted the importance of ambitious but realistic timetables that take into account a country's implementation capacity as well as the prevailing political and social environment.

Lessons and limitations. Directors welcomed the broad policy lessons for the IMF offered by the IEO case study of Jordan, while recognizing the limitations in distilling general policies from the experience of a single country. Directors noted that similar lessons have been drawn before, including in earlier IEO reports, and have resulted in a number of policy changes that have contributed to improving the effectiveness of IMF operations, including in Jordan. Directors urged the staff to pursue their efforts to ensure that the policy changes introduced in these areas continue to be implemented as effectively as possible across the entire membership.

D. Financial Sector Assessment Program

Overview

This evaluation assesses the effectiveness of the Financial Sector Assessment Program (FSAP) from the perspective of the IMF. A parallel evaluation by the World Bank's Independent Evaluation Group (IEG) (formerly OED) assesses the World Bank's role. The FSAP was established in 1999 to provide advice to strengthen the financial systems of member countries by facilitating early detection of financial sector vulnerabilities and helping to identify financial sector development needs. Although a voluntary program, it has become the principal platform for financial sector diagnosis at the IMF. It is a joint IMF-World Bank exercise (except in industrial countries), but with different outputs for different purposes, including a confidential report to the authorities and separate summary reports to the Boards of the IMF (the Financial System Stability Assessment or FSSA) and the World Bank (Financial Sector Assessment or FSA), dealing with issues that are in their respective areas of responsibility.

The evaluation's conclusion is that the FSAP represents a distinct improvement in the IMF's ability to conduct financial sector surveillance and in understanding the key linkages between financial sector vulnerabilities and macroeconomic stability. It has significantly deepened the IMF's understanding of the financial sector in specific countries, helped articulate policy recommendations, prompted better discussions with authorities, and helped support policy and institutional changes. The FSAP also permits an integrated approach to assessing financial sector vulnerabilities and development needs that could not be achieved by an ad-hoc series of assessments of standards or analysis of particular issues. The evaluation also suggests that the joint IMF-World Bank nature of the exercise has been generally beneficial.

The evaluation suggests some significant advantages of the present arrangements that should be preserved going forward: (i) an integrated approach to assessing financial sector vulnerabilities and development needs; (ii) an institutional link to surveillance that has greatly strengthened the operational relevance of the FSAP for IMF activities; and (iii) an administrative mechanism to coordinate IMF and World Bank inputs. Thus, while a variety of channels to strengthen financial sector surveillance are clearly possible and would be relevant in particular country circumstances, the evaluation evidence suggests that FSAPs and comprehensive Updates offer distinct advantages that would be difficult to replicate fully through other less comprehensive modalities. These advantages derive largely from the critical mass of expertise mobilized for an FSAP which enables comprehensive assessments of financial systems and interaction of country officials with a range of technical experts.

Despite these achievements, the initiative is at a critical crossroads and there is a danger that some of the gains could be eroded without significant modifications. The evaluation indicates two related sets of problems. First, financial stability assessments have not yet been fully "mainstreamed" as a regular part of IMF surveillance. Second, looking beyond the stage of initial FSAPs, there are serious doubts that current incentives for participation and associated priority-setting procedures will suffice to ensure coverage of systemic and vulnerable countries where a strengthening of financial sector surveillance may be most needed. The evaluation also points to the need for changes in the way the IMF organizes its own activities in order to make the best use of scarce technical expertise as well as to a range of measures that would further improve the quality and effectiveness of FSAPs.

Key findings and recommendations

The evaluation's major findings and related recommendations are focused on three key themes: (i) reconsidering incentives for participation, clarifying priorities, and strengthening the links with surveillance; (ii) steps to maintain and strengthen further the quality of the FSAP and organizational changes within the IMF; and (iii) the working of the joint IMF-World Bank approach. Although the recommendations are couched in terms of actions to be taken by the IMF, the joint nature of the initiative makes that a number of them could require decisions by both the IMF and World Bank Boards.

Incentives for participation, clarifying priorities, and strengthening the links with surveillance

Priority setting within the FSAP was bound to be a complicated exercise because of: (i) the initiative's multiple objectives and (ii) tension between the voluntary nature of the exercise and the stated priority to be given to systemic importance and potential financial sector vulnerability. The evidence from the evaluation suggests that, in practice, the multiplicity of objectives has not so far prevented priority being given to countries of systemic importance and/or with potential financial sector vulnerability concerns, provided such countries agree to participate. However, greater clarity is needed on how the balance between IMF-driven and World Bank-driven priorities will be resolved in the longer term. The evidence also suggests that there is increasing tension between the voluntary nature of the initiative and systemic coverage. This is not so much because a minority of systematically important countries have not yet volunteered (although they certainly should be encouraged strongly to do so), but because a significant number of countries that should be high priority candidates for updated assessments have been reluctant to participate in a timely manner. In addition, the evaluation shows that the IMF is not yet using the FSAP results as effectively as it could in its overall surveillance activities.

These findings suggest the need for changes in how country choices for financial sector assessments are made and in how those assessments are mainstreamed into IMF surveillance. The approach proposed by the IEO contains the following mutually-supporting elements: country-specific strategies for financial sector surveillance that choose between a range of modalities for such surveillance, including FSAPs and Updates, based on sharper criteria for priority setting (Recommendation 1); strengthened incentives to encourage comprehensive assessment exercises when they are judged necessary for effective surveillance, albeit within a still-voluntary framework for the FSAP (Recommendation 2); and strengthened links between FSAPs and Article IV surveillance (Recommendation 3). The overarching idea is that, to maintain its strong relevance to the IMF’s global surveillance objectives, financial sector assessments and their updates should cover most countries of systemic importance and/or with potential financial vulnerabilities in a timely manner. Both the incentives for participation and priority-setting criteria should be set with this objective in mind, and the IMF should take stock periodically of progress, drawing on explicit benchmarks for achieving adequate country coverage.

Recommendation 1. The IMF Board and management should refine the criteria for setting priorities on IMF resource inputs into financial sector surveillance, including the FSAP. Based on these priorities, IMF staff should indicate, as part of its medium-term planning, what components are needed for strengthening financial sector surveillance in each country, drawing upon a range of possible modalities. These strategies would form the basis for more explicit accountability on results.

Going forward, if incentives for participation are strengthened successfully, clearer guidance (and division of primary responsibilities within the existing coordinating framework) will be needed on how to manage the resource tradeoffs between following-up at relatively frequent intervals on vulnerability issues in countries of systemic importance (or where there are warning signs concerning the financial sector) and a more extensive examination of financial sector development issues in lower income countries.

Country-specific plans to guide financial sector surveillance should address two basic questions: (i) how much priority and emphasis should be given to financial sector issues in surveillance (considering explicitly the systemic importance and macro-relevance of potential financial sector vulnerabilities) and (ii) what is the frequency, scope and modality of assessments that would best fit each country's circumstances and the relative priority accorded to these issues. When domestic or international aspects of financial stability are of critical concern, the country-specific plans should involve stronger efforts to "mainstream" financial sector assessments into the focus of regular Article IV surveillance.

Recommendation 2. **To strengthen incentives and drawing upon these country-specific plans, IMF management should clearly signal to the Board those countries that it sees as the highest priorities for FSAPs and Updates, irrespective of whether these countries have volunteered. These lists should be the basis for periodic discussions by the Board of country-specific priorities**.

Moreover, in cases where there are indications of potential financial sector vulnerabilities in systemically important countries that have not volunteered for an initial assessment or Update, IMF management should indicate to the Board where it proposes to call for an intensified analysis of financial sector issues as part of the regular Article IV surveillance.

Country coverage of the FSAP should be reviewed again after several years to asses whether the proposed strengthening of incentives has been effective. If the Board concludes at that time that coverage is falling significantly short of the bulk of countries signaled as high priorities, consideration should be given to shifting to a more mandatory approach.

Recommendation 3. Strengthen the links between the FSAP and surveillance by mainstreaming FSAPs and follow-up work into regular surveillance activities. This means incorporating the assessment of financial sector standing and vulnerabilities into the overall macroeconomic assessment of the country in a way that fosters a greater understanding of stability; policy recommendations that are set in a coherent framework combining macroeconomic and financial sector analysis; more meaningful discussion of financial sector issues with authorities; and enhanced peer review discussion at the Board. This would require, inter alia, strengthening the internal review process, giving FSAP team leaders a greater "voice" at the time of Board discussions, and the Board itself seeking greater attention to financial sector issues in its surveillance discussions when the FSSA flags significant macro-relevant issues.

Improving the quality and impact of the FSAP and organizational changes

While the evaluation concludes that the overall average quality of the FSAP exercises is quite high, several shortcomings were identified. The most systematic shortcoming was the insufficient attention paid to cross-border financial linkages and their potential consequences. In addition, problems were encountered in many FSAPs with inadequate prioritization of recommendations, as well as insufficient indication of the degree of urgency of implementation. These problems hampered effective follow-up by both surveillance and technical assistance.

Moreover, while the application of various analytical tools significantly strengthened the overall quality of assessments, problems were encountered in a number of areas: (i) a tendency to understate the potential consequences of identified weaknesses in supervisory standards (especially with regard to de facto enforcement rather than de jure regulations); (ii) presentations of stress-testing results that tended to overstate what the exercises could say about the soundness of financial systems (given data and methodological constraints) which, in some cases, was compounded by a reluctance to investigate politically sensitive shocks; (iii) in a minority of cases, there was insufficient integration of the macroeconomic and financial sector components of the assessment; and (iv) many authorities would have liked to see greater efforts by FSAP teams to understand the political economy context of their country and to structure recommendations—especially those concerning wide-ranging reforms—with this context in mind.

Recommendation 4. **Implement steps to improve further the quality of the FSAP and strengthen its impact**. In most cases, these steps would involve applying more systematically what is already current policy or "good practice." This would include for example clearer prioritization of recommendations and candid discussion of the potential consequences, more systematic inclusion of cross-border/financial sector issues, and greater involvement of the authorities in the overall process, including a written response.

Recommendation 5. Introduce changes in the organization of IMF mission activities to utilize scarce financial sector technical expertise (especially in MFD and ICM) more effectively in the surveillance process.[15] This may require changes in the way surveillance missions are organized, in the direction of a model in which the area department is the strategic coordinator of relevant specialist inputs provided by functional departments.

Joint IMF-World Bank nature of the FSAP

The evaluation found that the use of joint IMF-World Bank teams (as well as outside experts) contributed significantly to the depth of analytical expertise and credibility of the findings. But if steps to strengthen incentives for participation are successful, then more concrete guidelines will be needed on how to manage tradeoffs between more frequent update assessments of countries of systemic importance and/or potential financial vulnerability and assessments of countries with less developed financial sectors.

[15] The ICM and MFD Departments were recently merged into one, the Monetary and Capital Markets Department (MCM).

The evaluation also indicates that there is often a weak framework for formulating detailed action plans to follow up on the FSAP recommendations, and identifying coordinated technical assistance support for these plans. While the country itself should take the lead to formulate such action plans, the IMF (and World Bank) can strengthen their support by better prioritization of recommendations in the FSAP and more explicit discussion of follow-up plans at the end of the FSAP exercise.

Recommendation 6. Maintain the current joint approach, but clarify further the distinctive contributions the IMF and Bank can make, with the IMF taking the lead where significant domestic or global stability issues are present, and the Bank taking the lead where financial sector development issues are more paramount. Such clarity should include a clear delineation of primary responsibilities for setting priorities (and contributing resources).

Recommendation 7. **The IMF, in conjunction with the World Bank and other technical assistance providers, should seek to establish a clearer framework for coordinating follow-up capacity-building technical assistance activities, based on the country's own action plans**. Establishment of such a framework will require a clearer understanding between the two institutions of the appropriate dividing line between the FSAP as an assessment vehicle and capacity building/development activities.

Executive Board response

The IMF's Executive Board discussed the evaluation report on January 27.[16] Executive Directors saw the IEO report as a key input into the IMF's efforts to strengthen financial sector surveillance, in line with priorities identified in the IMF's medium-term strategic review and the McDonough report.[17] Directors agreed with the evaluation's key conclusion that the FSAP represents a distinct improvement in the IMF's ability to conduct financial sector surveillance. Directors were encouraged by IEO's assessment that FSAPs and updates help articulate policy recommendations, prompt better discussions with authorities, and help support policy and institutional changes. Some Directors especially noted the finding that FSAPs often had an impact on the internal policy debates. At the same time, Directors concurred that the main challenges relate to "mainstreaming" the FSAP into bilateral and multilateral surveillance and to ensure participation by countries where financial surveillance is most needed.

[16] The Summing Up of discussion can be found at *www.imf.org/ieo/2006/fsap/eng/pdf/sumup.pdf*

[17] The McDonough Report, titled "Report of the Review Group on the Organization of Financial Sector and Capital Markets Work at the IMF" provided the IMF with an independent perspective on how it should organize its financial sector and capital market analysis and surveillance activities. The review was led by William J. McDonough, former President of the Federal Reserve Bank of New York. The report has not been made public.

Incentives for participation

Most Directors agreed with the report's assessment that incentives to participate in the

FSAP are critical for maintaining the effectiveness of the program. They were concerned that some countries that are systemically important and/or may have vulnerable financial systems still have not volunteered for initial assessments or for updates. However, most Directors considered that the voluntary nature of the FSAP should be maintained.

Recommendation 1. While some did not see sufficient evidence that current mechanisms are inadequate, many Directors agreed on the need for clearer guidance—including on the trade-off between assessments of vulnerability and development issues—as part of a medium-term strategy aimed at efficient resource allocation in line with the IMF's core mandate.

Recommendation 2. Most Directors agreed with the IEO proposal that, to better align FSAP coverage with the needs of surveillance, management should indicate to the Board which countries it considers the highest priorities for FSAP assessments and updates. Annual reporting on participation could provide useful information to guide discussion of priorities.

Recommendation 3. Directors concurred with the recommendation to strengthen links between FSAPs and surveillance. They underscored the need to follow up on key vulnerabilities and gaps and integrate such issues into Article IV surveillance reports. Directors stressed that in cases where financial stability issues, including any potential global repercussions, are judged to be of high importance, they should be a major focus of Article IV consultations.

Improving quality and impact

Recommendation 4. Directors encouraged the staff to follow up on IEO recommendations to improve further the quality of FSAPs and strengthen their impact. They noted that recommendations should be clearly prioritized and the potential consequences candidly discussed. Directors emphasized in particular the importance of treating financial sector and cross-border linkages more systematically in FSAP analysis.

Recommendation 5. Many Directors welcomed the IEO's recommendation to introduce changes in the organization of IMF mission activities to utilize more effectively scarce financial sector expertise within the IMF. Directors noted that this will be considered in the broader context of improving financial sector surveillance, as part of the medium-term strategic review.

Bank-IMF collaboration

Recommendation 6. Directors were in broad agreement with the recommendations regarding Bank-IMF collaboration. They concurred that the current joint approach, including the central role for the Bank-IMF Financial Sector Liaison Committee (FSLC), should be maintained. At the same time, further efforts should be made to take full advantage of the distinctive contributions that the two institutions can make—with the IMF focusing on stability issues and the Bank on financial sector development and institution building.

Recommendation 7. Directors concurred that there is room to improve the coordination of FSAP-related technical assistance activities, based on the country's own action plan. At the same time, Directors cautioned against overburdening the FSAP with additional expectations regarding the technical assistance needs.

E. Multilateral Surveillance

Overview

Surveillance is a core function of the IMF, a critical element of its toolkit to promote global financial stability. Multilateral surveillance brings into analysis economic linkages and policy spillovers between countries, as well as international economic and market developments. It complements bilateral surveillance by adding global and cross-country perspectives to the analysis of developments in individual countries. And by exploring options to deal with policy spillovers in a global context, it can enhance the policy advice that the IMF gives to its members.

The IMF is not alone in analyzing the world economy; a number of other government bodies and private entities do so as well. What is special about the IMF is that its near-universal membership gives it a uniquely broad and in-depth perspective. Moreover, all IMF member governments have committed themselves to be part of a system of peer review and oversight. To be influential in this environment, IMF multilateral surveillance must bring to bear analytical rigor, clear policy prescriptions, and an active engagement with senior national policymakers and relevant international forums.

Owing to the substantial cost to the IMF of multilateral surveillance, and the key role that the IMF plays in ensuring a more stable world economy, the IEO conducted an evaluation of the IMF's multilateral surveillance activities for the period 2000–05. Its evaluation report commends the analytical quality of the individual components of multilateral surveillance but sees considerable scope for better coordinating these components. The IEO report offers several suggestions for improving the effectiveness of multilateral surveillance.

The IEO evaluation addresses a number of questions about multilateral surveillance:

- Do the multilateral surveillance issues analyzed correspond to the IMF's unique perspective with respect to economic linkages between countries?

- Are the issues examined relevant and timely?

- Does multilateral surveillance enhance the policy advice provided by bilateral surveillance?
- How well are macroeconomic and capital market surveillance combined in the analysis of relevant issues?
- Do the messages of multilateral surveillance reach the intended audience?
- Are the messages being presented in a way that maximizes their impact?

To answer these questions, the IEO reviewed public and internal documents drafted between 2000 and 2005. It also surveyed or interviewed IMF staff, officials from several governments and international organizations, market participants, and academics at universities and research institutes.

Key findings

Most of the components of multilateral surveillance products were found to be well crafted and to feature high-quality analysis; they were also useful to particular audiences and for satisfying particular needs. The World Economic Outlook (WEO) is especially well regarded. The evaluation report, however, cites the lack of a clear and comprehensive strategy to guide the integration of the components and the delivery of outputs. Because of this, multilateral surveillance is falling short of its full potential.

The absence of an overall strategy has meant that IMF multilateral surveillance as a whole is less than the sum of its parts. Outputs give too much weight to descriptive information on economic developments and prospects, for which the IMF is increasingly only one of many sources. They give too little weight to analyzing economic policy linkages—in which the IMF has a comparative advantage—and to proactively identifying scope for collective, international action. In addition, the current set-up for involving the Executive Board in multilateral surveillance limits the Board’s contribution.

The IMF’s failure to clarify the operational goals of multilateral surveillance and to define the mechanisms to best meet them has resulted in:

- a predominantly “bottom-up,” or country-based, approach to policy advice;
- a “silo” structure, in which different IMF departments produce different outputs without adequate coordination. This hinders the fuller integration of macroeconomic and capital market approaches;
- a proliferation of publications that lack focus; and

- an insufficiently proactive engagement with various high-level groups of national policymakers.

Content and quality

Selecting issues for analysis. The products of multilateral surveillance—especially the WEO—have been largely successful in selecting for analysis issues that reflect the IMF's comparative advantage (see Box 2.1). The WEO gives roughly equal weight to issues that deal with the spillovers of policies in individual countries and to analyzing and comparing the experience of different countries. Dedicated analysis of exchange rate issues and related spillover effects, however, does not appear frequently—which is surprising given the IMF's mandate to oversee the international monetary system and the exchange rate policies of its member countries.

Box 2.1. The Main Outputs of IMF Multilateral Surveillance

IMF multilateral surveillance is disseminated to various audiences through a number of outputs, including:

- semiannual "flagship" publications: the World Economic Outlook and the Global Financial Stability Report;
- semiannual regional outlooks produced and published by four IMF area departments; and
- regular contributions to intergovernmental forums and committees, such as the Group of Seven (G-7), the Group of Twenty (G-20), and the Financial Stability Forum.

In addition, IMF staff prepares several documents for internal use as well as for IMF management and the Executive Board.

Identifying relevant issues and global risks. The WEO has also succeeded in identifying in a timely way relevant issues for analysis, as measured against the issues subsequently picked up on Group of Seven and Group of Twenty agendas. In terms of identifying relevant global macroeconomic and financial risks, both the WEO and the Global Financial Stability Report (GFSR) also compare favorably with similar publications of other international and national bodies. This assessment, however, is based on evidence gathered during the relatively calm period of 2000–05, when no major crisis tested the IMF's "early warning" mechanisms.

Integrating multilateral and bilateral surveillance. The IEO evaluation confirms the finding of a 1999 external evaluation of surveillance[18] that IMF surveillance has a strong bilateral (or country) orientation. As a result, policy advice and economic forecasts predominantly reflect the views of IMF area departments (the departments—grouped by geographic

[18] The External Review of IMF Surveillance, commissioned by Chairman of the Executive Board's Evaluation Committee, Tom Bernes, was undertaken by a team of outside experts, including Ricardo Arriazu, a former alternate IMF Executive Director; John Crow, former Governor of the Bank of Canada and the Chairman of the External Review Team; and Niels Thygesen, the Danske Bank Professor of International Economics at the University of Copenhagen. The report is available on the IMF website (www.imf.org).

region—that carry out bilateral surveillance). Because of this country orientation, multilateral surveillance has not sufficiently examined options to deal with policy spillovers in a global context. Moreover, the language of multilateral advice is no more based on explicit consideration of economic linkages and policy spillovers than that of bilateral advice. In addition, the dominant bottom-up (or individual country) approach also tends to yield consistently optimistic macroeconomic forecasts for certain regions.

Integrating macroeconomic and capital market analysis. The insufficient integration between the WEO and the GFSR noted in the IEO evaluation report is also emphasized in the recent McDonough Report mentioned earlier. The evaluation identifies areas where integration could have been desirable but did not take place, largely owing to the "silo" structure of multilateral surveillance.

Use and delivery

Use of the WEO and GFSR in bilateral surveillance. The evaluation finds that most area department economists do not make much use of the WEO in their country work (other than the WEO's quantitative forecasts of major economic variables). Only 14 percent of IMF senior staff surveyed said that WEO topics were discussed with national authorities. Substantial scope thus exists for IMF staff to increase its use of multilateral surveillance outputs in its bilateral surveillance.

Similarly, few area department economists (4 percent) use the GFSR on a regular basis in their country work. Although the GFSR has raised some important longer-term issues, it has not in practice added value to bilateral surveillance beyond the information already available in the markets. And it has not adequately distilled the implications of market developments for the IMF's day-to-day country work.

Presenting the message. Given the variety of tasks assigned to multilateral surveillance products, the reports have become too long and unfocused. In the case of the main surveillance chapter of the WEO (Chapter I), for example, each component of the analysis may be useful to a particular audience or meet a particular need, but the effort to meet all the varying demands has expanded the chapter unduly. Indeed, the full WEO document could benefit from considerable streamlining to highlight its critical messages. As to surveillance notes, which the IMF prepares as input for G-7 and G-20 meetings, these should concentrate on spelling out the consequences of policy spillovers and the options for addressing them.

Reaching the intended audience. Attempts to reach multiple audiences through the same publications have complicated the task of communicating the WEO and GFSR messages. The wide press coverage enjoyed, particularly by the WEO, indicates that IMF multilateral surveillance messages have a significant potential for influencing public debate. Yet, the IEO evaluation team was struck by the low readership (both internally and externally) of the full WEO report, with most readers relying only on summaries. This underscores the need for the products of IMF multilateral surveillance to have a more explicit "customer" focus, with a range of well-communicated products aimed at meeting the diverse needs of various IMF audiences.

Exploiting the potential for peer pressure. The potential for multilateral surveillance to exert peer pressure on individual country policies is not fully realized. First, the IMF is not proactively engaged with the G-7, the G-20, or in other forums to which it has unique access. Second, the current structure for involving the Executive Board limits the contributions that it, and the IMFC, can make to multilateral surveillance.

Evidence of effectiveness

The ultimate test of the effectiveness of the IMF's multilateral surveillance is its impact on policies in member countries. Are such policies ever modified as a result of IMF advice about linkages and spillover effects, or as a result of discussions or peer pressure in international forums to which the IMF provides analysis and advice? Answering this question is difficult for several reasons, including the multiple factors that influence a country's policy choices. The evaluation report identifies a few specific instances where policy debate or policymaking was influenced by IMF multilateral surveillance:

- *Risk transfer to household balance sheets.* The IMF introduced this issue at a meeting of the Financial Stability Forum. Several officials told the IEO evaluation team that the IMF material influenced their preparation for the meeting.

- *Global imbalances and oil prices*. Officials in several countries cited recent IMF analyses on these issues as having informed internal debate in their countries. Policymakers said that the IMF work was for the most part timely and valuable in developing their own thinking.

- *House prices*. A WEO analysis of house prices spurred debate in at least one large European country about house price rises across Europe.

- *Foreign direct investment in financial services*. One G-7 official said that an IMF staff member contributed a great deal of detailed knowledge to a meeting of the Basel-based Committee on the Global Financial System. Another official called the IMF's contributions useful and timely.

More generally, the IEO evaluation team found that many of the policymakers interviewed agreed that IMF multilateral surveillance could be a valuable input into national and global economic policymaking if it is conducted and communicated effectively.

Recommendations

To improve the effectiveness of multilateral surveillance, the evaluation report recommends that the IMF:

Recommendation 1. Strengthen the IMF's role at the center of a more robust global peer review system by establishing a more proactive engagement with relevant intergovernmental groups.

Recommendation 2. Enhance the roles of the Executive Board and the IMFC in multilateral surveillance.

Recommendation 3. Streamline and better focus the products of multilateral surveillance, present shorter and clearer messages, and deliver them more strategically to target groups.

Recommendation 4. Define more clearly the goals of multilateral surveillance and the mechanisms to achieve them. Particular effort should also go into better integrating multilateral perspectives into bilateral surveillance.

Executive Board response

In discussing the IEO evaluation report on March 24, 2006,[19] Executive Directors welcomed the broadly positive assessment of the analysis in the IMF's key multilateral surveillance outputs. They also noted that multilateral surveillance products had been largely successful in identifying relevant issues and related risks in a timely manner. The wide and diverse public interest in these outputs, documented by the IEO's report, is a testament to this success. Directors discussed ways to improve the effectiveness of multilateral surveillance, based on the IEO's four recommendations.

Directors agreed that it would be beneficial to clarify the operational goals of multilateral surveillance, but they were not persuaded about the need for broad organizational changes. Priority should be given to strengthening the integration between multilateral and bilateral surveillance, particularly for countries that have an impact on global financial stability.

Directors noted that multilateral surveillance outputs would have a larger effect on the global policy debate if they were better targeted to their core audiences, streamlined, and focused on key issues.

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[19] A full Summing Up of the Board discussion, as well as the responses by IMF management and staff to the evaluation report, can be seen on the IEO website (www.imf.org/ieo) and are also included in the print version of the report.

Most Directors concurred that, while the Executive Board and the IMFC remain the most appropriate forums for discussing policy spillovers and possible responses, the IMF should also participate more actively in other forums—such as, but not limited to, the G-7 and the G-20—which provide opportunities for a frank exchange of views on multilateral issues.

III. STATUS OF ONGOING PROJECTS

This section describes the main features of three evaluations currently underway. The first two, Structural Conditionality in IMF-Supported Programs and The Role of the IMF in Determining the External Financing Envelope in Sub-Saharan African Countries, are nearing completion whereas work on the third on IMF's Advice on Exchange Rate Policy began in spring 2006.

A. Structural Conditionality in IMF-Supported Programs

The use of structural conditionality (SC)—involving changes in policy processes, legislation, and institutional reforms—by the IMF gained prominence in the late 1980s and rose significantly in the 1990s with the emergence of new lending facilities for low-income countries (whose main objective was the removal of obstacles to growth) as well as the new challenges posed by the transition economies. SC also became important as the IMF increasingly recognized the need for structural reforms to achieve sustainable results in macroeconomic and financial areas. More recently, SC gained importance as a signal to other sources of finance, such as multilateral agencies, bilateral donors and private capital markets.

The proliferation of structural conditions in the 1990s was met with strong criticism outside the IMF. It was argued that many structural conditions were not needed for the achievement of program goals, and that there was not a clear division of labor between the IMF and the World Bank. In addition, it was argued that there were areas where the IMF had become too "ideological," such as privatization and trade reforms.

Largely in response to this criticism, the IMF launched in 2000 a "streamlining initiative" aimed at reducing the volume and scope of SC. Subsequently, the IMF issued in 2002 new conditionality guidelines, stressing the need for parsimony in the use of conditionality and including a test of "criticality" for any variable selected for conditionality (i.e., to be included in a program, conditions must be "critical" for the achievement of a program's objectives). The guidelines also stress the need to seek national ownership of programs and for programs to reflect the authorities' policy goals. Programs supported by the PRGF are expected to be based on the PRSP resulting from a broad consultative process within the country.

Issues addressed by the evaluation

- How has SC worked in practice in different types of arrangements? Under what conditions has it helped in promoting medium-term structural reform? What is the role of country ownership and what are the views of the authorities on the negotiation process? How do country-specific initial conditions and program design issues interact with each other in determining outcomes? Can best practices be identified in the area of SC design (i.e., practices leading to a better process of interaction with the authorities and more effective SC)?

- To what extent is SC addressing multiple objectives? Has SC been excessive or overused, or has it been the wrong instrument of engagement in particular circumstances?

- Are there general areas of collaboration between the IMF and the World Bank that require particular attention so that both can better contribute to structural change? What is the experience of SC in supporting privatization and what are the links with World Bank operations in this area?

- What has been the effect of the streamlining initiative and the 2002 Conditionality Guidelines on the numbers and direction of SC? Are there areas of increased or reduced emphasis, and why? Has the process of setting SC become more strategic and focused, and better linked to program objectives? How well is SC linked to a long-term policy framework in the case of PRGFs?

Methodology

The evaluation uses various techniques to address the issues:

- To study the rationale for SC and assess whether SC helped structural reforms, the evaluation examines in depth 13 arrangements approved in 1999–2003 and completed by 2005, which account for about 17 percent of all structural conditions set in that period. The sample includes a mixture of regular stand-by arrangements (precautionary and non-precautionary), and PRGFs. In addition, evaluation teams visited five of countries in the sample. In the other cases, the authorities were contacted to assess their views on the process of negotiation.

- To examine the impact of the streamlining initiative the evaluation uses a cross section of data on all structural conditions in programs approved in the 1995–2004 period, as well as desk studies of post-streamlining arrangements to assess the criticality test, and a survey to examine how staff is interpreting the guidelines and elicit their views on the effects of the streamlining initiative.

B. The Role of the IMF in Determining the External Financing Envelope in Sub-Saharan African Countries

This evaluation examines IMF experience in assisting low-income Sub-Saharan African countries in determining their external resource envelopes. Recent years have seen calls by the international community for more and better aid to help countries achieve the MDGs and related development goals. With higher levels of aid being committed by major donors—especially for Sub-Saharan Africa—identifying the lessons that can be learned from past experience with different aid flow levels becomes increasingly important. The evaluation builds on an earlier IEO evaluation of the IMF’s role in PRSPs and PRGFs, which was completed in 2004.

The IMF influences the external resource envelope in low-income countries primarily through PRGF financial program design, which implicitly determines how much available aid can be used, and through its dialogue with donors. Both channels have attracted criticisms by external observers. These critics contend that IMF assumptions about aid absorptive capacity and availability tend to be too conservative, imparting a negative—and, they argue, frequently self-fulfilling—bias to PRGF program design and donor flows, which in turn reduce country prospects for growth and poverty reduction.

Against this background, the evaluation zeroes in on the features of PRGF program design and implementation that relate to aid inflows. Its analytic framework focuses on aid absorptive capacity—both its underlying macroeconomic, fiscal and debt sustainability, governance, and sectoral dimensions and the integration of those dimensions (and the tradeoffs across them) into a coherent assessment. Noting that the World Bank, among others, plays a central role in carrying out much of the relevant sectoral and governance analysis, the evaluation also looks at how well IMF-supported programs drew on the expertise and analysis of partners. It also documents how and in what circumstances IMF-supported programs have catalyzed donor funding and affected aid predictability.

Issues for evaluation

As set out below, key evaluation questions being addressed consider how IMF staff approached the diagnosis of aid absorption capacity and availability; the implications of PRGF program design for the availability and use of aid; and, where feasible in light of timing considerations, program outcomes:

- *Diagnostics.* The evaluation focuses on how IMF staff analyzed the underlying macroeconomic and sustainability dimensions of aid absorptive capacity and took into account the analyses of the World Bank and others of the sectoral and governance dimensions. It also asks whether and how staff integrated these different dimensions into an overall assessment of country aid absorptive capacity that was in turn reflected in the PRGF's financial program. Looking at the supply of aid, the evaluation examines how staff formulated the program's aid projections and how they took into account aid modalities, volatility, as well as upside and downside risks.

- *Program design.* The evaluation takes an ex-ante perspective for much of the analysis of program design. In so doing, it considers: (a) the stance of policies in the program, including with respect to the utilization of aid; (b) whether the program drew on the full array of thinking and intellectual capital available at the time; (c) how well the program accommodated available aid and dealt with its uncertainty; and (d) how the program addressed the need for policy/institutional changes to strengthen absorptive capacity if the latter was a binding constraint to program design. The evaluation also looks at IMF staff's dialogue with and signals to donors, including in cases where projected aid flows fell short of absorptive capacity.

- *Outcomes*. Where the timeframe permits, the evaluation also takes an ex-post perspective. It looks at what was actually achieved under the program in terms of growth and poverty reduction, and—mindful of the methodological complexities—tries to identify the IMF's contribution to these outcomes through its influence on program design, policies, and aid levels.

Methodology

The evaluation utilizes several sources of evidence. Where data and methodology permit, quantitative analyses—covering the sample of 29 Sub-Saharan African countries with completed or lapsed PRGF programs—are being carried out. For about half these countries, in-depth desk analyses of program documents are being undertaken, with country visits planned in some cases. The latter will allow for structured interviews with the authorities, country-based donor agencies, civil society, research institutions, and others, complementing surveys of these groups in all sample countries as well as IMF and World Bank staff. Structured interviews are also being planned for donor headquarters.

C. The IMF's Advice on Exchange Rate Policy

The IMF was created with a key mandate to promote exchange stability and prevent competitive exchange rates depreciation. Originally, the IMF was the guardian of the system of fixed (but adjustable) exchange rates. In 1978, the Articles of Agreement were amended to allow each member the freedom to choose its exchange rate regime and, as a result, IMF's role was changed. The IMF assumed an obligation to exercise surveillance over the effective operation of the international monetary system and members' obligations under Article IV.[20] In turn members undertook to collaborate with the IMF to promote a stable system of exchange rates and to avoid manipulating exchange rates or the international monetary system to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members.

Since then, surveillance has largely evolved into a form of policy dialogue between the IMF and its members, with the IMF's view on advice on exchange rate policies becoming the subject of considerable debate. The IMF's view has been that exchange rates are only one element of economic policy and must be seen in this overall context. The IMF's views on exchange rate regime choice seems to have shifted after major crises, and currently the IMF is seen by many as strongly favoring a flexible exchange rate underpinned by inflation targeting as the only viable regime under most circumstances. In this contest, some critics have charged that the IMF has become less willing to express clear views on exchange rate issues and that it should be more open to other types of arrangements better attuned to country-specific considerations.

[20] The IMF's Articles of Agreement are available at http://www.imf.org/external/pubs/ft/aa/aa.pdf.

Issues for evaluation

The Independent Evaluation Office (IEO) is undertaking an evaluation of the IMF's advice on exchange rate policy broadly defined to include any IMF advice on exchange rate issues, particularly those relating to members' regime choice and sustainability, and to measures directed at resolving or avoiding currency misalignment and external imbalances.[21] On the basis of this definition, the evaluation seeks to answer the following overarching questions:

- Is the role of the IMF in exchange rate policy advice clearly defined and understood?
- What has been the quality of IMF advice on exchange rate policy? Has it kept up with best practice and structural changes in global capital markets?
- Have multilateral perspectives adequately complemented the bilateral assessments?
- Has the dialogue with country authorities been effective?
- What has been the impact of IMF advice on exchange rate policy?

Exchange rate surveillance is a continuous process. For each "cycle," however, the process of providing advice on exchange rate policy can be represented by a multi-stage "results chain" that connects "inputs" with IMF activities and their outcomes. The questions above are being examined along the different stages of the chain, namely (i) analysis and assessments; (ii) communication of policy advice (including review by the Executive Board); and (iii) follow-up, including continuous monitoring between cycles. Each stage embodies bilateral and multilateral components, which we consider to be two complementary perspectives inherent to any surveillance activity.

In asking these questions, the IEO hopes to enhance transparency and contribute to ongoing discussions on how best to conduct exchange rate surveillance. Although exchange rate surveillance has been frequently reviewed within the IMF, internal reviews have not assessed the content of policy advice per se, as called for by the Executive Board during the 2002 and 2004 Biennial Surveillance Review discussions. This evaluation seeks to shed light not only on the process of surveillance, but also on the content of the advice itself. It intends to be as forward looking as possible, and thus it has chosen to place the focus on the 1999–2005 period (following the East Asian crisis) but in line with the IEO's terms of reference it will not make judgments on the IMF's policy advice currently being given in specific country cases.

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[21] On June 26, 2006, the IEO posted the final issues paper for this evaluation on its website incorporating comments from Executive Directors, staff, and the public, which is available at http://www.imf.org/External/NP/ieo/2006/erp/eng/041906.pdf.

Methodology

The evaluation is drawing on multiple sources of evidence including a desk review of the IMF's public and internal documents and interviews with staff, country authorities, Executive Directors, and other stakeholders, including academics and market participants. The evaluation may also conduct a survey of national authorities, members of the Executive Board, and IMF staff.

The evaluation work is proceeding with a review of the latest Article IV staff reports for all member countries (and economic areas), while at the same time a more selective, but intensive, review of a limited number of economies (Table 3.1) will be conducted. In addition, the evaluation team will visit a number of these economies to gather the views of the authorities and the private sector on the work of the IMF. Work on the soundness of certain analytical tools used by the IMF will also be undertaken.

Table 3.1. Sample Countries for the Evaluation 1/ 2/

Africa	Asia-Pacific	Europe	Middle East and Central Asia	Western Hemisphere
CEMAC/WAEMU	Australia	Bulgaria	Egypt	Brazil
Guinea	China	*Euro Area*	Morocco	Ecuador
Rwanda	Hong Kong SAR	Iceland	Saudi Arabia	El Salvador
South Africa	Japan	Lithuania		Jamaica
Tanzania	Korea	Norway		Mexico
	Malaysia	Russia		Peru
	Singapore	Ukraine		United States
		United Kingdom		

1/ Italicized entities refer to regional monetary unions.
2/ The regions correspond to the geographical jurisdictions of IMF area departments.

IV. LOOKING AHEAD: THE IEO WORK PROGRAM AND FUTURE MENU OF TOPICS

Under the IEO terms of reference, the Director of the IEO makes a final decision on the work program following consultations with Executive Directors, management, and staff, as well as with informed and interested parties outside the IMF. In April 2006, the IEO circulated to the Board and published on its website a list of 23 possible topics for evaluation which had been elaborated in consultation with various stakeholders.[22] Feedback was sought and received from many quarters on both the substance of the suggestions and on priorities of timing. Subsequently in July, the Director identified four additional projects to be added to the IEO work program. The selection reflected many factors, including judgment on overall importance, the balance of issues, and appropriate timing, as well as the degree of public criticism. In particular, IEO priorities, as well as timing, are significantly affected by the fact that several topics are now being reviewed in other contexts.

The following four projects were added to the IEO's work program (Table 1) in July 2006:

- Aspects of IMF Corporate Governance—including the Role of the Board
- The IMF's Interactions with its Member Countries
- The IMF's Research Agenda
- The IMF's Approach to International Trade Issues

The main issues to be covered in these four projects are described below. Following IEO practice, detailed issues papers will be prepared for each project and the IEO will seek comments from internal and external stakeholders before the scope of each evaluation is finalized. The final terms of reference will also be posted on the website and concerned stakeholders will be invited to submit substantive inputs on any aspect of the terms of reference.

Depending on their scope and complexity, the new projects would likely be completed in FY2008 or the first half of FY2009. The precise timing and ordering of the new projects will depend in part on the availability of appropriate staff resources as they are recruited or freed up from current projects. The remaining topics from the original list will be held over for consideration, together with other potential topics, to be included in a work program at a later stage.

[22] Available at http://www.imf.org/External/NP/ieo/2006/mt/eng/050806.pdf.

A. Aspects of IMF Corporate Governance—Including the Role of the Board

Corporate governance is the way in which organizations are directed and controlled. It defines the distribution of rights and responsibilities among the different stakeholders and participants in the organization, determines the rules and procedures for making decisions on corporate affairs including the process through which the organization's objectives are set, and provides the means of attaining these objectives and monitoring performance. During the last 30 years, the world has witnessed dramatic changes both in the private sector—where many firms have significantly changed their lines of business, organizational structure, size and operating technologies—and in the public sector—where in many national governments, institutions have undergone significant adjustments in size, mandate, programs, organizational structures, and internal operations.

Some have argued that the IMF has not kept up with changes witnessed in other organizations. Most of the current arrangements defining the corporate governance of the IMF—including the relationships between the IMFC, the Board, and Management—have remained mostly unchanged for many years. At the same time, there has been significant evolution in communications between capitals, groupings of countries,[23] the Board, and the IMF in general. The IMF has also become a more transparent organization. Some critics have argued that the Board exercises relatively little influence over management and is unable to ensure accountability of staff and management. Others have argued that the Board exercises too much control and is itself unaccountable. The evaluation would assess how the current structure has worked in practice. It would look at mechanisms for consultation and allocation of decision-making responsibilities between the Board, management and staff as well as the relative roles of the IMFC, Deputies and groupings of countries. Underlying processes would be evaluated against the purposes of the institution, political accountability, and efficiency of decision-making.

While the concept of corporate governance can potentially cover a large area, the principles underpinning a strong corporate governance framework are often summarized in terms of four values—equitable treatment, responsibility, transparency and accountability. This evaluation would focus in particular on the relationships and interactions among staff, management and the Executive Board. It would not address the ownership structure of the IMF itself.

The evaluation would draw upon the expertise of a multidisciplinary team. While keeping in mind the sui generis nature of the IMF, an important element would be a benchmarking of the IMF corporate governance structure with that of other international organizations as well as relevant government and private sector organizations.

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[23] See Leo Van Houtven (2002) available at http://www.imf.org/external/pubs/ft/pam/pam53/contents.htm for an introduction to the "Governance of the IMF".

B. The IMF's Interactions with its Member Countries

The effectiveness of the IMF depends in large part on a successful relationship between the IMF and its member countries. The IMF comprises the Executive Board, management, and staff, and while most of the interaction with member countries takes place between the staff and the country authorities, messages delivered by the Executive Board and other channels of interaction have become increasingly important in recent years. In particular, greater efforts have been made to establish contacts between staff (either headquarters-based or resident representatives) and non-government institutions (parliamentarians, civil society, market participants, the press, etc.) in member countries. The evaluation would focus on how the relationship between staff and country authorities is working, but would also investigate how other channels of contact have affected that key relationship.

A starting point would be to establish how well the nature of the relationship is understood by various parties, including an understanding of the appropriate interactions given the unique set of rights and obligations inherent in IMF membership. Thereafter the study would examine the nature of the interactions. In some cases the relationship is perceived to be working very well and the study would attempt to identify underlying best practices, including why some regions have been more receptive to the IMF's efforts. In other cases there is frequent criticism that the IMF too often conveys advice and views to country authorities without adequately taking account of country circumstances, or without listening carefully enough to the views of the authorities. As a result, critics contend, the IMF does not form an accurate assessment of the true needs and priorities of the membership, or, even when broadly correct, is insufficiently specific to be helpful. It thereby misses opportunities to be effective, or, even worse, misdiagnoses problems or recommends inappropriate policy advice.[24]

A second type of criticism is that even when the IMF's views are carefully considered and well worth listening to, they are conveyed in a way that is unlikely to be effective. Either the written documents are too long and inaccessible to be widely used, or contacts are not made with sufficiently senior officials, who, in some instances, are simply unaware or misinformed about the IMF's purpose and the nature of its activities. Relatedly, it is sometimes claimed, the IMF, while being much more transparent in recent years, has not proactively used the opportunities to shape opinion in member countries that could facilitate debate and reform of economic policies.

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[24] Under this type of criticism falls charges that the IMF is arrogant in its views; adopts a "one-size fits all" approach to problems that are diagnosed in Washington; adopts the latest policy priorities of key members or donors, rather than those of the country it should be advising; or is oblivious to the political and technical constraints that are critical in designing and implementing policies.

The study would rely on various sources, including (i) a perception survey of senior officials in member countries; (ii) in a sample of countries, structured interviews with officials as well as parliamentarians, representatives of the private sector and nongovernmental organizations; and (iii) a survey of relevant staff, management, and Executive Directors. Based on the views of country authorities and others, the project could evaluate whether the IMF's engagement with member countries could be more effective. It would examine aspects of IMF country operations across a wide array of instruments, including program relationships, Article IV consultations, and technical assistance and training, and the modalities of interaction, including through missions, resident representatives, and communication with headquarters. The evaluation would attempt to assess how well the IMF's instruments and modalities of operation are aligned with the needs of policymakers, and how well the relationship with member countries is managed.

C. The IMF's Research Agenda

Six years ago, a group of independent experts evaluated the IMF's economic research activities.[25] At that time, the Executive Board agreed with the group's finding that there was "substantial room for improvement in the overall quality of the IMF's research." Among other conclusions, Directors endorsed the recommendation that the mix of research conducted at the IMF would need to be directed more to areas where it could add the most value and agreed that it could be integrated to a greater extent into policy work—an assessment that has also been shared by external critics of the IMF. The evaluation would be a follow up exercise and look at two areas.

- First, the evaluation would examine the way in which research topics are selected and priorities imposed across the IMF, and the extent to which the recommendation has been carried out to direct research more to areas where it could add the most value and be better integrated into policy work. In order to do this, an analysis of the research conducted by all departments in the IMF would be undertaken, using as a starting point the work performed by the existing interdepartmental Research Committee. The evaluation would attempt to identify which pieces of research had been particularly relevant and influential for the country and policy work of the IMF. In addition a survey of staff and country officials would try to elicit whether some topics could have received greater priority. Given the attempt to streamline and focus IMF activities in recent years, and to seek ways to save costs—issues that will be of even greater importance in the years to come—the evaluation would explore the extent to which decisions on research topics are guided by the opportunities to rely on research conducted outside the IMF, either at other institutions such as the World Bank and the OECD, or in academia.

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[25] See http://www.imf.org/external/pubs/ft/extev/res/index.HTM.

- Second, the evaluation will investigate aspects of the quality (as opposed to the scope and relevance) of IMF research. The process by which IMF research is supervised and vetted would be examined. The views on a sample of research would be sought from a panel of external experts. Issues such as the degree of innovation, and the consistency with first best methodology would be studied.

D. The IMF's Approach to International Trade Issues

A stated purpose of the IMF is to facilitate the expansion and balanced growth of international trade.[26] Last year's internal staff review of the "IMF Work on Trade"[27] concludes that the IMF has consistently advocated open trade regimes as a means to improve economic efficiency, combat rent-seeking and corruption, and promote income growth. While providing a broad overview of the IMF's work on trade policy, including conditionality, the internal review has not sought to address far reaching questions relating to the appropriateness and effectiveness of the IMF's advice on trade reforms. During the review's discussion at the Board, directors generally agreed that it would be desirable to conduct case studies on the impact and design of trade policy reforms recommended by the IMF. They considered such studies helpful for drawing lessons for future country-specific policy advice and program design.

The IMF's approach to trade has always drawn substantial criticism. According to critics, (i) IMF-supported trade liberalization has been too fast, (ii) programs have not included appropriate social safety nets for affected vulnerable parts of the population, (iii) IMF advice on trade liberalization has ignored market imperfections in domestic and world markets, (iv) the IMF has failed to take into account the impact of tariff reductions on the revenue base and fiscal sustainability, (v) trade conditionality has been driven by the agenda of developed country shareholders in the IMF, (vi) IMF requirements to liberalize unilaterally has decreased program countries' bargaining power in the multilateral negotiations, and/or (vii) the IMF has been too soft on tariffs and non-tariff barriers in industrial countries as well as on other policies of industrial countries that amplified global trade imbalances.

The evaluation would entail in-depth case studies of program, surveillance, and technical assistance activities focusing on IMF involvement in trade reforms and their impacts. It would assess the quality and effectiveness of the IMF's advice at country, regional, and multilateral levels, as well as on global trade imbalances. It would also look at the IMF's coordination with other organizations like UNCTAD, UNDP, World Bank, and the WTO (all of which have their own respective mandates in the area of trade). In the light of the recent decisions—at the last Annual Meetings of the IMF and the World Bank as well as the

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[26] See Articles of Agreement of the IMF available at http://www.imf.org/external/pubs/ft/aa/aa.pdf.

[27] See http://www.imf.org/external/np/pp/eng/2005/020705.htm.

last WTO Ministerial Meeting—to enhance the *Integrated Framework for Trade-Related Technical Assistance to least developed countries* (IF),[28] this evaluation would include the IMF's contribution to the work of the IF since its inauguration in October 1997. The Evaluation would complement the evaluation of the World Bank's trade policy advice recently carried out by the Bank's Independent Evaluation Group.[29]

[28] See http://www.integratedframework.org/.

[29] See http://www.worldbank.org/ieg/trade/report.html.

Objectives and Modes of Operation of the IEO

A. Purpose of the IEO[30]

The purpose of the IEO, as outlined in its Terms of Reference, is to systematically conduct objective and independent evaluations "on issues, and on the basis of criteria, of relevance to the mandate of the IMF." The terms of reference further elaborate that the IEO is intended to:[31]

- Serve as a means of enhancing the learning culture of the IMF;
- Strengthen the IMF's external credibility;
- Promote greater understanding of the work of the IMF throughout its membership; and
- Provide independent feedback to the Executive Board in its governance and oversight responsibilities over the IMF.

The work of the IEO is envisaged as complementing the review and evaluation work being conducted within the IMF and is expected to improve the IMF's ability to draw lessons from its experience and to more quickly integrate improvements into its future work.

B. Independence

Independence of evaluation is critical if it is to be credible. This aspect of evaluation was emphasized in the Executive Board discussions that led to the establishment of the Independent Evaluation Office. The Terms of Reference explicitly state that the "IEO will be independent of IMF management and staff and will operate at arm's length from the IMF's Executive Board." The following provisions are designed to achieve this objective:

- The Director of the IEO is appointed solely by the Executive Board, IMF management, while it may be consulted in the selection process, is not involved in

[30] Additional background to the thinking behind the goals and mode of operations of the office is given in "Making the IMF's Independent Evaluation Office Operational: A Background Paper," prepared by the Evaluation Group of Executive Directors, August 7, 2000 (www.imf.org/external/np/eval/evo/2000/Eng/evo.htm).

[31] For the full terms of reference of the IEO, see http://www.imf.org/external/np/ieo/tor.htm.

making the selection.[32] The Director is specifically precluded from appointment or reappointment to an IMF regular staff position at the end of the term of office.

- With a view to ensuring that the IEO is staffed with independent and highly qualified individuals, the Director of the IEO is solely responsible for the selection of IEO personnel, a majority of whom must come from outside the IMF.[33] IEO staff report exclusively to the Director of the IEO and not to IMF management.

- The budget of the IEO is prepared by the Director and submitted directly to the Executive Board for approval. IMF management is not involved at any stage of the process.

- The IEO's work program is determined by the Director in light of consultations with members of the Executive Board and other interested stakeholders, from both inside and outside the IMF. The work program determined by the Director is presented to the Executive Board for review, but is not subject to the Board's approval.

C. Transparency and Accountability

The IEO has developed procedures which allow for extensive consultations in designing each evaluation project and also for receiving substantive inputs during implementation.

To ensure consultation at the design stage, each evaluation begins with the preparation of an issues paper that identifies the questions to be addressed and, to the extent possible, the methodology to be followed. The issues paper is posted on the IEO website (www.imf.org/ieo) to elicit comments from a wide set of interested external observers. The IEO also seeks comments from Executive Directors, IMF staff and management, and member country governments (especially in the case of evaluations involving individual countries). The comments received are taken into account in determining the final terms of reference for the study, which is also posted on the website.

The responsibility for the research undertaken and the conclusions reached must necessarily rest with the IEO. However, in conducting its evaluations the IEO interacts extensively with concerned parties both inside and outside the IMF. A unique feature of IEO evaluations, which distinguishes it from other external analyses of IMF activities, is that the IEO has access to internal IMF documents not normally made public and can also interview IMF staff concerned with the subject of the evaluation. For evaluations involving individual countries,

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[32] The initial terms of reference provided for a four-year term, renewable for a second term of up to three years. In November 2004, the Board modified these terms to provide for a single nonrenewable terms of six years. The new Director, Mr. Thomas Bernes, was appointed on these terms in June 2005.

[33] The maximum length of appointment for full-time staff in the IEO is six years.

consultations are held in the country concerned with both the authorities and a broad range of other interested parties, including civil society. Furthermore, the issues paper posted on the IEO website specifically invites interested parties to make submissions to the IEO on issues covered by the issues paper.

An important aspect of transparency and credibility is the assurance that IEO reports will be published and disseminated to a wide audience. The IEO's Terms of Reference provide that the reports, once they have been considered by the Executive Board, will be promptly published "unless in exceptional circumstances the Executive Board were to decide otherwise." All evaluation reports prepared by the office have been published.

To ensure full transparency, IEO reports are published in the form in which they were submitted to the Executive Board, without being changed in any way in light of comments received from management.[34] Comments received on the evaluation report from IMF management and staff, along with the IEO's reactions to those comments, if any, are submitted to the Executive Board as separate documents for the Board meeting at which the evaluation report is discussed. These documents are published together with the evaluation report and a summary of the Executive Board discussion. Once released to the public, the report is immediately posted on the IEO's website, followed by publication of the print version.[35]

[34] The only exception would be for purely factual corrections, for which an errata page, identifying the specific corrections made, would be issued.

[35] A full list of IEO publications is available on the IEO website at www.imf.org/external/np/ieo/pap.asp.

Revised Administrative Budget: Independent Evaluation Office
(In current U.S. Dollars) 1/

	FY2005		FY2006		FY2007
	Budget	**Outcomes 2/**	**Revised Budget 3/**	**Projected 4/**	**Budget**
Total	**4,300,147**	**3,727,515**	**4,459,850**	**4,457,383**	**4,530,786**
Regular staff allocation 3/	2,800,380	2,436,953	2,902,420	2,902,420	3,074,600
Of which:					
Contractual staff (temporary fill-in of vacancies) 3/			...	109,364	
Discretionary Budget	1,373,100	1,198,082	1,426,203	1,444,963	1,320,366
Experts and contractuals 5/	860,600	759,171	891,203	935,841	825,067
Business travel and seminars	500,000	433,404	523,000	491,352	483,299
Other fungible budgets	12,500	5,507	12,000	17,770	12,000
Publications	126,667	92,480	131,227	110,000	135,820

1/ In this presentation, the IEO's budget includes the costs of publications, which previously had been treated as part of a centrally managed budget.

2/ The outcome for 2005 excludes the cost of the search for the new IEO Director ($96,000).

3/ The original FY2006 budget was increased by $82,280. This amount had been netted from the initial budget proposal reflecting an average expected vacancy rate IMF-wide. The projected outturn for FY2006 makes full use of the regular staff allocation.

4/ As of July 13, 2005.

5/ Excludes contractual staff under regular staff allocation.

IEO Outreach Seminars and Workshops in 2005–06

The IEO seeks to reach as broad an audience as possible in its outreach efforts, consistent with its budgetary constraints. The following is a list of events in which IEO staff participated in 2005 and the first four months of 2006.

January 17–19, 2005, Johannesburg, South Africa
Presentation on PRGF/PRSP evaluation at Strategic Partnership for Africa seminar

February 8, 2005, Washington, DC, U.S.A.
Discussion at the Institute for International Economics on capital account liberalization.

March 16, 2005, London, U.K.
Workshop on TA evaluation results attended by officials and NGOs.

April 23–27, 2005, Tokyo, Japan
Workshop on PRSP/PRGF evaluation at the Ministry of Finance, attended by senior officials and academics who are members of the advisory panel on MDBs.

August 15–16, 2005, Rabat, Morocco
IEO Director’s consultations with authorities on IEO role and activities.

August 17, 2005, Tunis, Tunisia
IEO Director’s consultations with authorities on IEO role and activities.

August 18–19, 2005, Algiers, Algeria
IEO Director’s consultations with authorities on IEO role and activities.

August 25, 2005, Beijing, China
Presentation at the People’s Bank of China on capital account liberalization.

October 10, 2005, Singapore, Singapore
IEO Director’s consultations with authorities on IEO role and activities.

October 13–14, 2005, Bangkok, Thailand
IEO Director’s consultations with authorities on IEO role and activities.

November 1–2, 2005, Berlin, Germany
International Experts Meeting on IEO evaluation projects, jointly hosted by Capacity Building International, Germany (InWent) and the IEO. Focus was on the capital account liberalization, TA, and FSAP evaluations.

November 7–8, 2005, London, U.K.
Consultations with NGOs, senior officials, and academics on IEO role and activities.

November 28, 2005 Abu Dhabi, U.A.E
IEO Director's consultations with authorities on IEO role and activities.

December 12–13, 2005, Zurich, Switzerland
Presentation on the role and activities of the IEO.

December 14, 2005, Berne, Switzerland
Seminar on capital account liberalization.

February 22, 2006, Basle, Switzerland
Seminar on FSAP at the Bank of International Settlements.

February 26, 2006, Bangkok, Thailand
Seminar on FSAP sponsored by the Bank of Thailand.

April 21, 2006, Washington, D.C., U.S.A.
Workshop on the IMF's Role in the Determination of the External Resource Envelope in Sub-Saharan African Countries, organized by IEO.

May 15, 2006, Washington, D.C., U.S.A.
Informal Workshop to discuss the IEO's Evaluation of the IMF's Advice on Exchange Rate Policy, May 15, 2006, organized by IEO.

TERMS OF REFERENCE FOR THE EXTERNAL EVALUATORS OF IEO
SEPTEMBER 14, 2005

Purpose of the evaluation

As foreseen in the terms of reference of the Independent Evaluation Office (IEO), the Executive Board has decided to initiate an external evaluation of the IEO. The purpose of the evaluation is to assess the effectiveness of the IEO and to consider possible improvements to its structure, mandate, operational modalities, or terms of reference. The main points of reference for the assessment are the IEO's goals, as set out in its terms of reference, namely to:

- serve as a means to enhance the learning culture within the IMF;
- strengthen the IMF's external credibility;
- promote greater understanding of the work of the IMF throughout its membership;
- support the Executive Board's institutional governance and oversight responsibilities.

Focus of the evaluation

In assessing the IEO's goals as set out in Section 1, the evaluators are requested to give particular attention to the following topics:

(i) *Independence of the IEO*. The actual and perceived independence of the IEO is a key element for its successful operation. Has the framework defining the relationships between the IEO, Management, and the Executive Board ensured its independence? Has the staffing of the office (internally and externally recruited personnel) and of the evaluation teams (full-time IEO personnel and external consultants) contributed to its independence? How independent are IEO evaluations perceived inside and outside the IMF?

(ii) *Topics for evaluation*. The IEO terms of reference contains only very broad guidelines regarding the choice of evaluation topics. Has the choice of topics been appropriate in view of the IEO's goals, as set out in Section 1, and the IMF's institutional needs? How has the broad-based consultation process worked in defining evaluation topics? Has the guideline regarding the avoidance of interfering with operational activities or attempting to micro-manage the institution been effective? Is there an appropriate division of labor between the IEO, the Office of Internal Audit, and the self-evaluation efforts? Should the IEO's role in assessing the IMF's organizational structure and internal processes be strengthened?

(iii) *Conduct of evaluation*. Providing the opportunity for different parties to comment an evaluation before its finalization while ensuring its independence constitutes a difficult trade-off. How have these issues been dealt with?

(iv) *Evaluation results*. The effectiveness of independent evaluations hinges on the quality of the reports and the relevance and usefulness of their recommendations. How do target audiences (both internal and external) perceive the overall quality of IEO reports? Were the recommendations generally perceived as useful by staff, management, the Board, and external audiences? Was an appropriate balance achieved between generality and specificity of the recommendations? Are follow-up procedures sufficient to ensure effective implementation of approved recommendations? Should the IEO's role in monitoring follow-up be strengthened? Is the current number of evaluations appropriate in terms of the IMF's ability to react effectively to the recommendations? Have the IEO's dissemination and outreach activities within and outside the IMF been appropriate and effective?

Evaluators

The evaluation will be carried out by Ms. Karin Lissakers (Chairperson), Mr. Ishrat Husain and Ms. Ngaire Woods. They shall conduct their work freely and objectively and shall render impartial judgment and make recommendations to the best of their professional abilities. As noted in the IEO's terms of reference, an important element of the evaluation would be the solicitation of input from a broad range of stakeholders, both from the official as well as the non-governmental community.

Access to confidential information and protection of confidentiality

The evaluators shall have unrestricted access to interview staff, Management, and Executive Board members, as well as to access all relevant IMF and IEO documents, minutes, and internal staff memoranda needed to carry out their task.

The evaluators undertake not to disclose, deliver, or use for personal gain or for the benefit of any person or entity without the consent of the IMF, any restricted or confidential information in possession of the IMF that they receive in the course of the evaluation. The Chairman of the Evaluation Committee will request an appropriate officer of the IMF to review the draft evaluation report with the purpose of pointing out to the evaluators any inadvertent disclosure of restricted or confidential information.

The evaluators are free to request information from country authorities and other sources outside the IMF as they deem appropriate.

Evaluation report: publication, Executive Board consideration, and comments

The IMF reserves the exclusive right to publish the report, and the evaluators undertake not to publish any part of the report separately. The staff, Management, the Executive Board, and the IEO will have the opportunity to respond to relevant parts of the evaluation report in draft form, as well as in final form. Evaluators are free to take account of any comments on the draft evaluation report.

Comments on the final evaluation report shall be considered part of the official record. There is a strong presumption that the Executive Board will decide to publish the evaluation report, any comments thereon, as well as the conclusions of the Executive Board consideration of the report.

Resources and timing

The budget for the external evaluation of the IEO is expected to be US$175,000 (excluding any administrative support from Executive Directors or IMF/IEO staff that might be requested by the evaluators). Within this total, and in consultation with the Chairman of the Evaluation Committee, the evaluators may arrange for research assistant support. The IMF will provide administrative support for the external evaluation.

The evaluators shall be provided with a letter of engagement, setting forth the terms and conditions approved by the Chairman of the Evaluation Committee. The “Terms of Reference of the External Evaluation of the Independent Evaluation Office,” dated September 14, 2005, shall be attached to the letter and acceptance of the engagement by the evaluators shall also mean acceptance of the “Terms of Reference.” The engagement will expire with delivery of the evaluation report and its consideration by the Executive Board, or if the Executive Board determines that the engagement should be terminated for any reason.

Evaluators will begin work in September 2005; completion of the evaluation report is expected for January 2006. The evaluators will keep the Chairman of the Evaluation Committee informed of the progress of the work.

EVALUATION OF PROLONGED USE OF IMF RESOURCES: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP 1/

IEO Recommendation	Executive Board Response 2/	Staff Task Force Recommendations and Board Response 3/	Follow-Up 4/
Institutional Arrangements and Rationale for IMF Involvement			
Adopt an operational definition of prolonged use, as a trigger for enhanced "due diligence" (i.e. ex-post assessments and forward-looking consideration of "exit" strategies). The criterion could distinguish between general and concessional resources.	Directors saw merit in a definition to trigger greater due diligence. Many Directors noted that a definition should carefully differentiate low income-countries relying on concessional resources. Several Directors cautioned that a definition should not be interpreted as creating a new classification of member countries and that there should not be an a priori judgment that prolonged use necessarily implies a problem.	For general resources cases, prolonged users should be defined as countries that have spent seven or more of the last ten years under stand-by or extended arrangements, including precautionary arrangements, which was the definition used in the IEO evaluation. For concessional resources, enhanced assessment and strategy procedures would be triggered after a country has gone through two multi-year arrangements under concessional facilities.	Definition adopted. The Board reviewed the policy on longer term program engagement in May 2006. Directors agreed to make two changes in the LTPE definition. First, all members will now be considered as having LTPE if they have spent at least seven out of the last ten years under programs supported by the IMF. Second, time spent under precautionary arrangements that remain undrawn does not count toward LTPE, parallel to the treatment of members using the Policy Support Instrument. Semi-annual reporting of the incidence of prolonged use is taking take place on this basis.
Make greater efforts to judge whether countries are ready to implement credible programs and be more selective in extending financial support. Use of IMF Resources proposals should contain an explicit and frank assessment of the readiness of borrowers to implement programs.	Directors supported the recommendation that staff papers be more candid in assessing institutional capacity and ownership. They emphasized the importance of explaining downside risks and avoiding any bias towards overoptimism. Implementation of initiatives relating to ownership would be an ongoing process, sometimes involving difficult judgments, in particular regarding more selectivity in the provision of IMF financial assistance, where strong country ownership is lacking. A number of Directors stressed that greater selectivity should not imply giving up on difficult cases.	Efforts to improve program design should be accompanied by greater selectivity in extending IMF financial support, based in part on the assessment of implementation capacity and ownership.	Principal case-by-case follow-up will be through the internal review process and Board review of individual country cases, with periodic assessments as part of the regular conditionality review.
Aim to provide the international community with credible alternatives to IMF lending arrangements as a condition for other official flows.	Directors noted that it would be desirable to develop credible alternatives to indicate to the outside world the IMF's approval of members' policies and looked forward to a discussion of the signaling function. They noted need for care in preparation and consultation, including with the Paris Club.	The IMF should have effective ways to signal its views on policies to a country's donors and creditors outside a IMF-supported program. Article IV staff reports, Press Information Notices and "assessment letters" provide important vehicles. This topic should be taken further in the review of IMF role in low-income countries. Donors' and other lenders' concerns about burden-sharing should not lead to inappropriate lending decisions by the IMF.	The issue of signaling was taken up in the Board's subsequent discussion on Signaling Assessments of Members Policies, although it did not address all the relevant issues brought up in the evaluation. This review resulted in the discontinuation of Staff Monitored Programs for signaling purposes. The Board discussed the issue of signaling on several occasions in 2004–05, culminating in the establishment in October 2005 of the Policy Support Instrument, which provides policy support and endorsement to low-income countries that do not need IMF financing and whose policies meet the standards of upper credit tranche conditionality.

EVALUATION OF PROLONGED USE OF IMF RESOURCES: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONTINUED) 1/

IEO Recommendation	Executive Board Response 2/	Staff Task Force Recommendations and Board Response 3/	Follow-Up 4/
Programs for identified prolonged users should include an explicit exit strategy.	Directors stressed the desirability, where appropriate, of the elaboration of corrective measures as part of a conscious "exit strategy."	The proposed assessment and strategic planning exercises (see below) would include an explicit "exit strategy" where appropriate for ending prolonged use. An element of such a strategy would include helping countries widen their options for external financing.	Policy adopted, with an explicit definition of prolonged use as the trigger (see above).
Introduce a differentiated rate of charge for prolonged users as a signaling device.	The Board did not support a differentiated rate of charge for prolonged users.	Not recommended	Recommendation rejected. No follow-up necessary.
Program Design			
Specific operational procedures should be developed to ensure greater emphasis in program design on the domestic policy formulation process, in order to maximize ownership: (i) modify procedures towards the authorities having the initial responsibility for proposing a reform program; (ii) encourage a process whereby core program elements are subject first to a policy debate within the member's own political institutions; (iii) surveillance should help create a better understanding of what would be expected if a program should become necessary; (iv) more explicit discussion of major uncertainties and how policies would be adapted if things turn out differently.	Directors broadly agreed with the recommendations. Many Directors underscored that they should be seen as part of a broader effort to ensure greater effectiveness of programs. They saw a need for continuing effort to improve program design, which would draw on the fresh perspectives provided by the report.	IEO's recommendations were consistent with lessons emerging from recent country experience. The revised conditionality guidelines, 5/ incorporate many of the recommendations and provide the appropriate vehicle to put them into practice.	The internal 2005 review of the conditionality guidelines found that substantial changes have been made in the direction of increasing national ownership, and made suggestions to enable further progress in this direction. Key cross-country findings were also assessed in the review of EPAs discussed by the Board in May 2006.
Programs should emphasize key institutional changes and strengthening implementation capacity more.	Directors underscored the importance of increasing the effectiveness of technical assistance in support of institutional capacity building.	The Task Force recommended that ongoing efforts to address these issues in operational work should be enriched by future work on program design, including research efforts, focusing on links between structural reforms and program objectives.	Regular conditionality reviews will monitor progress. The August 2005 Review of PRGF Program Design examined the role of institutions in supporting growth and avoiding crises.

EVALUATION OF PROLONGED USE OF IMF RESOURCES: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONTINUED) 1/

IEO Recommendation	Executive Board Response 2/	Staff Task Force Recommendations and Board Response 3/	Follow-Up 4/
Greater selectivity in program content with: (i)further strengthening collaboration with the World Bank; (ii) a more differentiated use of conditionality; (iii) greater efforts to tailor the time frame of program design to foreseeable length of reform and adjustment; (iv) more in-depth analysis of real economy responses to key policy elements and less attention to fine-tuning financial programming.	Directors were encouraged that recommendations on streamlining of IMF conditionality and need for more effective collaboration with the World Bank were already being internalized as part of the review of conditionality.	The Task Force agreed with the IEO recommendations, many of which were already incorporated into the revised conditionality guidelines. Directors stressed importance of continued efforts to improve program design, including improved collaboration with the World Bank. Directors looked forward to further work by the staff on the relationship between external financing, adjustment, and sustainability; on the analytic framework for program design; on trade-offs between macroeconomic and structural policies; and on the parameters for assessing program success.	The 2005 review of the conditionality guidelines found major shifts in the coverage of structural conditionality, consistent with a greater focus on critical measures. Design of IMF-supported Programs, discussed by the Board in December 2004, examined in detail issues regarding program success, financing, adjustment and debt sustainability, analytical frameworks used in program design, and specific macroeconomic and structural policies.
Systematic ex post assessment of programs, with priority to identified prolonged users and key messages reported to the Board. Key internal database on program targets and outcomes (MONA) should be upgraded to facilitate such assessments.	Directors endorsed the recommendations.	The Task Force proposed that a process of ex post assessment and strategic planning would take place for all prolonged users, with lessons presented to the Executive Board.	Policy adopted. As of end-June 2006, 42 ex post assessments had been completed. A number of these assessments were led by staff from outside the area department. The MONA database is being upgraded.
Surveillance			
Steps should be taken to further strengthen surveillance in program cases. A case exists for greater institutional separation between surveillance and programs, especially in the context of prolonged use.	Regular IMF surveillance of program countries should reassess economic developments and strategy from a fresh perspective.	The Task Force agreed with the overall thrust of the IEO recommendations which it believed would be best addressed through continuing implementation and refinement of recently revised (i.e., 2002) surveillance guidelines. These guidelines proposed that surveillance should assess more carefully social and political realities; reach out more widely to legislative bodies and line ministries and ensure that timing of consultations is such as to enable them to influence policy. Directors concurred with the priority given to increasing effectiveness of surveillance, including the need to combine clarity and candor with recognition of social and political realities. They highlighted the importance of efforts to ensure that Article IV consultations in program countries "step back" from program context.	Progress will be monitored as part of regular biennial reviews of surveillance. At the 2004 review, Directors concluded that the quality of surveillance in program countries had improved since 2002. 6/

EVALUATION OF PROLONGED USE OF IMF RESOURCES: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONCLUDED) 1/

IEO Recommendation	Executive Board Response 2/	Staff Task Force Recommendations and Board Response 3/	Follow-Up 4/
Internal Governance Issues			
The ability of staff to analyze political economy issues should be strengthened.	Most Directors encouraged the staff to enhance its analysis and reporting of political economy issues in staff reports. Some Directors cautioned that IMF should be careful in venturing into this area, given its comparative advantage in technical analysis and the need to avoid intruding on internal political matters.	The Task Force recommended an effort to enhance reporting and analysis of political issues, when it has important implications for economic policy. Staff capacities could be strengthened through a modest investment in training.	Training courses in political economy have now been established.
Procedures should be evolved to help avoid the appearance of political interference in determining whether programs deserve support. All programs should be prefaced by an explicit assessment of implementation risks. When management suggests risks are high, the Executive Board should be given an opportunity to express on the record its own assessment of the tradeoffs.	Directors underscored the importance of distinguishing clearly between technical and political judgments and that staff should be candid in its assessment of risks.	The Task Force noted that there can be no question about the responsibility of management for recommending and the Executive Board for considering and approving, all requests for the use of IMF resources. Staff nonetheless has an important responsibility for providing candid technical assessment of risks and tradeoffs, and should continue to strengthen both substance and presentation of this material.	Greater candor on risks is being adopted in presentations to the Executive Board. Staff reports increasingly emphasize the risks to the IMF, including the political risks to implementation.
A review of internal incentives facing staff should be undertaken with a view to minimizing turnover of staff working on countries and to foster increased candor and accountability.	Recommendations are largely management responsibility. They have important implications for internal governance and deserve careful consideration.	While overall personnel policies do not need to be changed, management should consider guidelines and incentives to reduce excessive mobility in country teams. The best way to guard against excessive mobility would be to reestablish spare staff capacity to absorb changing demands.	The Human Resources Department, at the request of management, is developing a more centralized approach to mobility. As part of an effort to ensure appropriate incentives, the Human Resources Department, in collaboration with departmental senior personnel managers provides career counseling that emphasizes the acquisition of new competencies rather than frequent mobility.

1/ Following the Board discussion of the IEO report on September 23, 2002, management established a Task Force to follow-up on the recommendations contained in the evaluation report. The specific proposals of the Task Force were then discussed by the Executive Board on March 7, 2003.

2/ This column summarize the reaction of the Executive Board on each recommendation as reported in the summing up by the Chair. Readers are invited to refer to the full text of the summary of the discussion which is included in the published version of the report and can be accessed from the IEO website (www.imf.org/External/NP/ieo/2002/pu/index.htm).

3/ "Conclusions of the Task Force on Prolonged Use of IMF Resources," February 4, 2003. The Task Force report and the summing up of the subsequent Board discussion on that report are available at www.imf.org/external/np/pdr/ufr/2003/020403.pdf.

4/ The column on follow-up is meant to provide factual information on additional steps taken after the Board discussion of the Task Force report. It is not intended to be an evaluation of any follow-up by management or the Executive Board.

5/ "Guidelines on Conditionality," September 8, 2002. Available at www.imf.org/External/np/pdr/cond/2002/eng/guid/092302.htm.

6/ See Public Information Notice at www.imf.org/external/np/pdr/surv/2004/082404.pdf#pin.

EVALUATION OF THE ROLE OF THE IMF IN RECENT CAPITAL ACCOUNT CRISES: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Pre-Crisis Surveillance		
Article IV consultations should take a stress-testing approach to exposure to a potential capital account crisis, extending and systematizing existing approaches. Staff should assess the potential impact of itemized risks. Staff should develop greater understanding of political constraints on policy, in part through wider dialogue. Market views and political economy analysis should be reflected in staff reports.	Directors concurred with the overriding message of the report for surveillance: to strengthen the effectiveness of IMF surveillance by extending and systematizing current guidelines for assessing vulnerabilities. They supported the call to itemize major potential shocks. Directors emphasized that stress-testing should not be over-generalized and mechanical, but should focus on key risks facing a particular country. Most agreed that the IMF should develop greater understanding of political constraints on policy while cautioning that this should not lead to interference in domestic affairs. A number cautioned that this could be counterproductive if it causes staff to lose focus and press for policies and reforms that are not macro-critical. Most Directors saw great value in systematic discussions with the domestic and the international financial and business communities—but emphasized that the staff would need to assess private sector views critically.	The Board paper for the August 2004 Biennial Review of Surveillance noted that the IMF had substantially strengthened its capacity to identify vulnerabilities in member countries. In particular, it noted that balance sheet issues had received substantial attention in surveillance of advanced and emerging market economies, although various components of vulnerability assessments were not well integrated when presented in staff reports. Since then, the identification of balance sheet vulnerabilities has been highlighted as a key area in guidance to staff on surveillance, and methodological tools and training have been developed that will help gradually mainstream balance sheet analysis in IMF surveillance..
Management and the Executive Board should take additional steps to increase the impact of surveillance, including through making staff assessments more candid and more accessible to the public. In particular, there should be a presumption of publication for Article IV staff reports. A clear presumption of publication for country-related staff working papers should also be established. Biennial reviews of surveillance should focus on assessing the impact of surveillance on key systemic issues in major emerging market economies.	Directors strongly supported greater candor in the assessment of country risks and vulnerabilities in staff reports, building on the increase in candor that has already occurred. Nevertheless, Directors expressed a range of views regarding the potential conflict between candor and transparency, and the implications of the proposed shift from voluntary to presumed publication of staff reports. Many Directors warned that greater candor could adversely affect both the IMF's dialogue with countries and market confidence in the context of the publication of staff reports. Some of these Directors felt that what really matters is candor in face-to-face consultations with the key decision-makers in a country, rather than in the staff report. Many other Directors strongly supported presumed publication. These believed that concerns about candor are overstated, and that surveillance would be more effective in building ownership and influencing policy if IMF analyses and recommendations are made public. It was agreed that the Board would return to the issue of presumed publication of staff reports during the discussion on transparency. Many Directors were not in favor of shifting from voluntary to presumed publication of staff reports, but a number strongly supported presumed publication.	The May 2006 version of the Operational Guidance Note for staff on Document Publication notes that staff reports should be drafted independently of the authorities' publication intentions and should include the staff's candid assessment of risks, their frank views on the authorities' policy stance and their policy advice on all areas deemed relevant. Since July 1, 2004, publication of staff reports for Article IV consultations is now "voluntary but presumed." Moreover, the member's agreement to publish staff reports is now required for management to recommend a program with exceptional access to the Board. This policy was confirmed at the time of the June 2005 review of transparency policies. Rules regarding modifications of reports prior to publication (including deletions) were also tightened at that time. Moreover, publication of country-related staff working papers is not subject to the consent of the member countries concerned. Increasing the impact of surveillance is one of the key objectives of the IMF's Medium-Term Strategy (MTS) . Staff have been encouraged to develop regional and country-level outreach strategies for this purpose. A broader, institution-wide communications strategy will be brought to the Board in Spring 2007.
The Executive Board should agree on a systematic plan to provide institutional incentives for greater candor in the assessment of country risks and vulnerabilities, possibly including measures to give greater independence to surveillance teams.	Directors encouraged the provision of institutional incentives to the staff to facilitate candor.	Some area departments have experimented with having a different mission chief for Article IV consultations with program countries or have a senior staff member not assigned to the country concerned participate in Article IV consultation missions. Biennial reviews of surveillance will remain the main vehicle for assessing progress.

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Escalated signaling should be used when key vulnerabilities identified over several rounds of surveillance are not addressed. Such a policy would help strike the necessary balance between the role of the IMF as confidential advisor and its role as a vehicle for transmitting peer reviews on members' policies and for providing quality information to markets. Moreover, management and the Board should explore the possibility of seeking "second opinions" from outside the IMF as part of the surveillance process when the authorities disagree with the staff's assessment on issues that are judged to be of systemic importance. This would also serve as a building block for the idea of escalated signaling.	Many Directors considered that escalated signaling might be an idea worth pursuing. A number of these Directors reserved judgment on the suggestion until they had more information about how it would work. A few Directors felt that escalated signaling would undermine the IMF's role as confidential advisor, and doubted that it would help in preventing crises or designing more effective programs. Many Directors were not in favor of inviting second opinions from outside the IMF. Whereas some Directors considered that a second opinion would bring a fresh perspective that could help resolve differences of opinions with the authorities, many were concerned that it could encroach on the role of the Board, and undermine the work of the staff. A few Directors also noted that this approach has been tried and has failed.	There was no consensus in the Board on escalated signaling or second opinions.
Program Design		
A comprehensive review of the IMF's approach to program design in capital account crises should be undertaken. In particular, (i) greater attention should be paid to balance-sheet interactions and their consequences for aggregate demand; (ii) program design should allow for a flexible response, in case unfavorable outcomes materialize; (iii) conventional financial programming-based conditionality should be reviewed, and possibly adapted for capital account crisis circumstances; (iv) parsimony and focus should be basic principles of structural conditionality and crises should not be used for pushing reforms that are not critical to crisis resolution, however desirable they may be in the long run; and (v) there should be an agreed communications strategy, characterized by a high degree of transparency.	Directors endorsed these recommendations and hoped forthcoming staff papers on program design and balance sheet effects would give due attention to them. They endorsed the report's focus on the restoration of confidence, and the importance of balance sheet effects on key macroeconomic variables. The balance sheet approach should be closely linked to debt sustainability analysis. There should also be more work on twin (banking and capital account) crises. Directors agreed that design should allow for a flexible response to unfavorable developments; that the conventional financial programming conditionality should be reviewed; and that there should be an agreed communications strategy. Nevertheless, a few Directors cautioned against excessive emphasis on risks and alternative scenarios in program documents, since it would be difficult to know all risks upfront and since such emphasis could erode the program's effectiveness in building confidence in the chosen action plan.	The December 2004 review of the design of IMF-supported programs examined the analytical toolkit for program design; including tools for balance sheet and debt sustainability analysis, and the performance of these tools for macro projections underlying program design. In April 2006, staff also completed a review of whether there were any systematic differences between precautionary and non-precautionary programs in terms of policies, conditionality, and macroeconomic outcomes, and whether these differences were attributable to the nature of the arrangement or to the member's economic problems. In the context of designing programs for crisis prevention, a recent staff study found that during periods of heightened vulnerability, IMF financing over the preceding year as a share of short-term debt can be effective in lowering the likelihood of a crisis. The 2005 review of the conditionality guidelines found that substantial changes have been made in the direction of greater parsimony in structural conditionality, and made suggestions to enable further progress in this direction.
The IMF as Crisis Coordinator		
The IMF should ensure that financing packages provided in response to capital account crises are sufficient to generate confidence and be of credible quality. In particular, (i) packages should not rely on parallel official financing unless the terms of access are transparently linked to IMF-supported strategy; and (ii) terms for the involvement of other institutions providing parallel financing should be specified at the outset.	The Board agreed with the recommendation, while noting that there are limitations on the IMF's influence on other sources of financing. The Board stressed that the recently revised access policy must be observed and emphasized the importance of program credibility, not large financing packages, as the heart of IMF involvement. Directors fully supported the idea of moving toward more explicit procedures for collaboration with regional development banks and others and clear delineation of responsibilities, while noting that such procedures do not by themselves guarantee effective coordination.	

EVALUATION OF THE ROLE OF THE IMF IN RECENT CAPITAL ACCOUNT CRISES: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONCLUDED)

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Internal Governance Issues		
The IMF should be proactive in its role as crisis coordinator. In particular, (i) management should provide a candid assessment of the probability of success to the Executive Board and shareholders; (ii) management should ensure that the technical judgment of staff is protected from excessive political interference; and (iii) the nature of private sector involvement will have to be determined on a case by case basis. The IMF should play a central role in identifying circumstances where concerted efforts can help overcome "collective action" problems, based on meaningful dialogue with the private sector.	The Board endorsed the recommendations. While Directors were in favor of early involvement of the Board in program discussions, a number of them observed that the Board and major members should not seek to micro-manage the operational details of programs or influence IMF missions in the field. Many Directors attached particular importance to the early involvement of the private sector as an integral element of crisis resolution.	The new framework for exceptional access decisions provides a mechanism for encouraging more systematic early consideration of circumstances in which the success of a program would be enhanced by voluntary efforts to address collective action problems among private creditors and where steps to address an unsustainable debt burden need to be part of a strategy to restore growth and financial viability.
Human resource management should be adapted to develop and better utilize country expertise, including political economy skills, and to establish “centers of expertise” on crisis management issues. In particular, (i) the length of staff assignments should be monitored to ensure continuity of staff expertise and a critical mass of country expertise in each systemically important emerging market economy should be developed; (ii) Resident Representatives should play a more central role in surveillance and program design; and (iii) internal procedures should protect those who raise uncomfortable issues through proper channels, but consequently attract complaints from the authorities.	The Board generally agreed on the need for institutional change to ensure that the IMF is in a position to respond rapidly to member countries facing crises. Some Directors supported creation of centers of expertise in crisis management, whereas others put greater emphasis on mechanisms for drawing upon available expertise and experience in the event of a crisis. A number of Directors favored longer country desk assignments, while others noted the importance of staff mobility in broadening the experience and perspectives of the staff and maintaining its impartiality. Most Directors favored a greater role for Resident Representatives with a few noting that only relatively senior resident representatives would be sufficiently acceptable to the authorities to play such a role. Directors supported modification of internal guidelines and human resource procedures. They also noted that human resource issues are management's responsibility.	The Monetary and Financial Systems Department was reorganized, with steps taken to provide a center of expertise on banking crisis resolution issues. An Internal Task Force is reviewing broad strategic issues related to the IMF’s Resident Representative program. The Board paper for the August 2004 Biennial Review of Surveillance (BSR) called for a reassessment of mechanisms for staff rotation and mobility to achieve greater continuity in the policy dialogue, enhance mutual trust, and build up country-specific knowledge. Guidance issued to staff following the 2004 BSR highlights a number of steps to foster good policy dialogue with the authorities. The internal review process has also been strengthened to provide greater continuity, for instance through the mainstreaming of pre-brief meetings. The introduction by the MTS of three-year surveillance agendas providing a medium-term framework to guide staff’s work should also go a long way in providing the needed continuity.

1/ This column summarizes the reaction of the Executive Board on each recommendation as reported in the summing up by the Chairman of the July 16, 2003 Board meeting. Although care has been taken to ensure accuracy, readers are invited to refer to the full text of the summary of the discussion which is included in the published version of the report and can be accessed from the IEO website (www.imf.org/external/np/ieo/2003/cac/index.htm).

2/ The description of follow-up is intended to provide a factual indication of any additional steps taken since the Board discussion of the evaluation report. It is not intended to be an evaluation of any follow-up by management or the Executive Board. Where staff internal assessments have been made of relevant issues, these are reported but have not been subject to any independent confirmation by the IEO.

Evaluation on Fiscal Adjustment in IMF-Supported Programs: Recommendations, Board Response, and Subsequent Follow-Up

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Program Design and Internal Review		
Program documentation should provide a more in-depth and coherent justification for the magnitude and pace of programmed fiscal adjustment and how it is linked with assumptions about the recovery of private sector activity and growth. It will also facilitate the review process and discussions at the Board, as well as provide external audiences with a more convincing explanation for the rationale for the program and identify possible risks and subsequent corrective measures.	Directors supported this recommendation, and deemed that this initiative would instill greater discipline in program design, enhance transparency, and provide the public and the private sector with a more convincing rationale for the program, thereby helping to overcome political obstacles to implementation. Nevertheless, they recognized that uncertainties regarding key macroeconomic variables, particularly in countries in crisis, and concern about the implementation of policy measures and reforms complicate this task. A few Directors cautioned against spurious precision in such justifications, and others noted that the magnitude and pace of programmed fiscal adjustment may also reflect political constraints. Several Directors stressed the importance of better integrating debt sustainability analyses into program work. Directors looked forward to further staff analysis of growth projections in the context of program design discussions.	The Fiscal Affairs Department (FAD) has prepared a guidance note to staff on how reports might best present the appropriate size, pattern and composition of fiscal adjustment.
The internal review mechanism should place more emphasis on the early stages of the process. A more intensive process of brainstorming is needed at the time of the initial brief, and the brief should also articulate more clearly the basis for the fiscal program, and its links with debt sustainability issues.	Directors supported this recommendation. They welcomed management's recent initiative aimed at enhancing the effectiveness of the review process, which, *inter alia*, encourages early consultation between departments.	Following a recent assessment of the internal review process by a staff task force, management endorsed several changes to the process, including more systematic discussions of key issues prior to the preparation of briefing papers. In particular, pre-brief meetings that bring together originating and reviewing departments for a discussion of the main policy issues are required for all Article IV consultations and new program briefs.
Programs should give greater emphasis to the formulation and implementation of key institutional reforms in the fiscal area, even if (as is likely) they cannot be fully implemented during the program period. Programs should make stronger efforts to specify those structural reforms which should be carried out during the program horizon as part of a broader road map of priority reforms. This road map, and its prioritization, should ideally have emerged in the course of surveillance and be updated regularly as outlined below.	Directors agreed that key institutional reforms can be more critical for fiscal sustainability than short-term expenditure and revenue measures. However, they recognized that short-term measures are hard to avoid in many cases, especially if the immediate objective is economic stabilization. Medium-term institutional reform may be of particular relevance in countries that have achieved macroeconomic stability and where "second generation" reforms are necessary to foster growth and reduce longer-term vulnerabilities. Some Directors agreed with the report's suggestion that reforms should be broken down into those that require executive action, legislation, and capacity building. Directors, however, pointed out that in crisis situations, the pressing need to resolve the crisis may pose serious constraints on a medium-term approach. They reiterated the conclusion of the discussion on the Evaluation of the Role of the IMF in Recent Capital Account Crises (BUFF/03/125) that a crisis should not be used as an opportunity to force long-awaited reforms, however desirable they may be, in areas that are not critical to the resolution of the crisis or to address vulnerability to future crises. Careful judgment will continue to be needed to focus conditionality on those reforms judged critical while at the same time ensuring that adequate progress is made in addressing vulnerabilities and achieving the program's goals during the period of the arrangement, thus safeguarding the IMF's resources.	See below.

Evaluation on Fiscal Adjustment in IMF-Supported Programs: Recommendations, Board Response, and Subsequent Follow-Up (continued)

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Surveillance		
The surveillance process should be used more explicitly to provide a longer-term road map for fiscal reforms and to assess progress achieved. • In collaboration with the authorities, the IMF should clearly identify in surveillance reports the most critical distortions in a country's public finances from the perspectives of equity and efficiency.	Most Directors agreed that Article IV consultations should play a stronger role in identifying longer-term reform priorities and the causes of past failures in addressing fiscal problems, and that these analyses should inform subsequent program design. In this respect, the various initiatives to distinguish Article IV surveillance from program work are aimed at providing fresh perspectives.	A pilot exercise was conducted in 16 countries with a view to strengthening discussion of structural fiscal issues, building on fiscal strategy briefs produced by the FAD. Following on from this pilot, FAD now maintains and regularly updates fiscal strategy briefs for about 55 countries. These briefs can be used by area departments to inform discussions with the authorities on critical structural and institutional fiscal issues that can subsequently be covered in Article IV and program reports. In a number of countries, staff reports have included enhanced coverage of structural fiscal issues and prioritized agendas for reform.
• Such an analysis would provide a road map for fiscal reform in the future, with a clear sense of priorities. It would help to provide the basis for identifying critical reforms—particularly in areas where these reforms have been lagging—that would need to be addressed should IMF financing be required in the future. • The identification in advance of areas considered critical will allow the authorities flexibility in the timing and packaging of reforms which is often lost if these reforms are flagged at the last minute in the context of a crisis situation. This approach would also help foster greater domestic debate on key reforms and hence would encourage homegrown solutions and greater ownership. Early and clear prioritization of reforms is also consistent with streamlining objectives—it will avoid last minute bunching of reforms under crisis situations. • The analysis of fiscal reform priorities should be accompanied by an assessment of why certain important distortions were not addressed in the past and what lessons have been learned from past experience. This should include an effort to identify and unbundle the various constraints to critical reforms, including lack of technical capacity, areas where additional legislative action is necessary, and areas where key decisions from the executive branch are required. • Surveillance should include more systematic efforts to estimate the extent of tax evasion and tax exemptions, including the use of cross-country comparisons. • Public debt sustainability could help anchor the road map of fiscal reform priorities proposed above and to assess tradeoffs over time. At the same time, debt analysis provides a check of cumulative progress in improving fiscal systems that could also be reported in successive surveillance reports.	Some Directors considered the current framework of surveillance to be adequate for achieving the objectives of the IEO's recommendation. Directors also called for staff reports to set out in more detail the progress in implementing the recommendations of ROSC and technical assistance missions, as well as key reform priorities. Nevertheless, they underscored that the ultimate responsibility to develop a fiscal reform agenda resides with the individual country authorities, while the IMF should stand ready to provide advice. Directors also stressed that, consistent with the IMF's mandate, surveillance needs to focus on key issues of macroeconomic relevance, which will be different in each country, and should draw on the expertise of other institutions as appropriate. They encouraged the use of cross-country experiences and comparisons, including inputs from regional and multilateral surveillance, to assist in program design. Most Directors viewed Article IV consultations as the appropriate vehicle for staff to identify countries in need of an in-depth fiscal review, stressing that this identification process should be applied uniformly to all member countries of the IMF. In most cases, these needs could be accommodated through technical assistance and ROSCs.	

EVALUATION ON FISCAL ADJUSTMENT IN IMF-SUPPORTED PROGRAMS: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONCLUDED)

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Role of the IMF in Social Protection		
The IMF should clearly delineate the operational framework in which social issues will be addressed within program design in non-PRGF countries. This should include a clear indication of the IMF's responsibilities and activities in this area. The objective should be to assist middle-income countries to prepare and improve their institutional framework to allocate resources to critical social programs and to establish mechanisms to protect the most vulnerable groups in the face of external shocks and budgetary retrenchment. • The IMF could invite the authorities regularly during Article IV consultations to identify the existing critical social programs and social services that they would like to see protected in the event of adverse shocks. Participation on the part of the authorities would clearly be voluntary. • Successful implementation will depend heavily on having better and more transparent expenditure monitoring systems. On the basis of the priorities identified by the authorities, the IMF and the World Bank could join their accelerated efforts to reform public expenditure management (PEM) systems, specifically geared toward the social area, with a view to protecting the specified programs and spending categories. • This concrete application of the PEM initiative is particularly important because in many cases where there is an IMF-supported program the World Bank is also active with adjustment lending supporting the budget. • Surveillance would routinely report on these initiatives and their progress over time.	Directors agreed that an important aim of program design should be to protect critical social expenditures. However, they stressed, as recognized in the report, that the IMF should not become involved in the detailed selection and design of social policy; this task is outside both the IMF's mandate and its expertise. A number of Directors supported the IEO's call for updating of the 1997 guidelines that direct IMF work in the social area, in order to improve their clarity and effectiveness as an operational tool in protecting the most vulnerable from economic shocks and budgetary retrenchment. Other Directors, however, viewed the existing guidelines as adequate, and a few considered that the annual and medium-term budgets of non-PRGF countries already adequately identify critical social sector programs. These Directors recalled that the new framework for Bank-IMF collaboration on public expenditure issues should enhance countries' public expenditure reform strategies, including measures to protect critical social spending. Most Directors agreed with the recommendation that staff should inquire, during Article IV consultations, whether the authorities have identified social programs that they would like to protect in the event of a crisis, as they believed this would help dispel the criticism that IMF-supported programs unduly curtail social spending. A few others considered this recommendation impractical, as it would create significant costs and pressures for the authorities with little benefit.	During the discussions of the 2004 Biennial Review of IMF Surveillance, the Executive Board concluded that, "In members where shocks could have a sizeable impact on social conditions, most Directors were of the view that Article IV consultations and other contacts can offer an opportunity to solicit interested members' views on protection of social safety nets or of other priority expenditures in times of economic stress." The surveillance guidance note issued to staff in early 2005 calls for social and related issues—such as poverty, income distribution, social safety nets, and social expenditures—to be addressed, with due regard to principles of focus and selectivity. However, the guidelines do not mention the specific recommendation noted in the first bullet of column 1. 3/

1/ This column summarizes the reaction of the Executive Board on each recommendation as reported in the Acting Chairman's Summing Up of the August 29, 2003 Board meeting. Although care has been taken to ensure accuracy, readers are invited to refer to the full text of the summary of the discussion, which is included in the published version of the report and can be accessed on the IEO website at www.imf.org/External/NP/ieo/2003/fis/index.htm.

2/ The column on follow-up is meant to provide factual information on additional steps taken after the Board discussion. It is not intended to be an evaluation of any follow-up by management or by the Executive Board.

3/ See Surveillance Guidance Note, May 2005.

EVALUATION OF POVERTY REDUCTION STRATEGY PAPERS AND THE POVERTY REDUCTION AND GROWTH FACILITY: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP

IEO Recommendation	Executive Board Response	Follow-Up 1/
Aligning incentives and objectives		
1. Introduce greater flexibility in the implementation of the PRS approach to fit better the needs of countries at different stages of the process and with different capacities and political and administrative systems. Countries would be put more firmly in the driver's seat by determining themselves: i) How the policy formulation, implementation, and monitoring processes will be built up over time. Progress would be monitored against an explicit set of country-determined intermediate benchmarks. ii) What the output of these processes will be in terms of documents, with IMF process requirements minimized.	Directors broadly endorsed the recommendation, agreeing that the PRS approach will need to be implemented flexibly taking due account of country-specific circumstances and the core objectives of the PRS approach.	Several changes have been made to introduce greater flexibility. In addition to the shift in focus from the JSA to the Joint Staff Advisory Note (JSAN) (see below), the Annual Progress Report can now be more closely aligned with domestic processes, giving the country an opportunity to assess progress and set the agenda for the period ahead. In most cases, APRs will not be discussed by the IMF and World Bank Boards and will be distributed for their information only. The requirement that the PRS and the PRGF be fully consistent has been eased, with the aim of eliminating the need for last-minute formal adjustments to the strategy document.
2. Shift the emphasis of the initiative from the production of documents to the development of sound domestic policy formulation and implementation processes. This would involve the following elements: i) Build in greater results orientation. ii) Shift the emphasis of the incentives structure to achieving substantive changes in domestic policies and processes that are objectively measured.	Directors agreed that there should be less emphasis on document preparation and more on improving the capability of countries to develop and implement policies. Some Directors agreed that countries should set explicit criteria for judging progress toward key intermediate objectives, but many Directors cautioned that this should not imply excessive IMF involvement in assessing the country's decision-making process and should not establish an unwarranted direct linkage between such assessments and the IMF's lending decisions. Directors noted that further discussion was needed on how the IMF should react in cases where it believes that the pace of progress chosen is not ambitious enough.	JSANs (see below) are to provide constructive feedback to the authorities, focusing on a limited number of suggested key improvements that could be made to the strategy. This increased selectivity is intended to focus efforts on substantive changes in policies and processes.
3. Clarify the purpose of the Joint Staff Assessment and redefine the vehicle accordingly.	Directors called for a reformulation of the JSA with an emphasis on graduated rather than binary assessments.	The Board subsequently accepted the staff proposal to replace the JSA with a JSAN that focuses on providing feedback to the authorities on the PRSP and that drops the binary (yes or no) assessment of the suitability of the PRSP as a basis for concessional lending.

EVALUATION OF POVERTY REDUCTION STRATEGY PAPERS AND THE POVERTY REDUCTION AND GROWTH FACILITY: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONCLUDED)

IEO Recommendation	Executive Board Response	Follow-Up 1/
Clarifying the IMF's role and improving its effectiveness		
4. Clarify what the PRS approach implies for the IMF's own operations and strengthen the implementation of the agreed role. This would affect the following areas: i) IMF engagement in the PRS process. ii) PRGF-related activities including clarifying the IMF role where the PRSP does not yet provide an operational road map. iii) Streamline IMF documentation and Board scrutiny.	Directors agreed that the IMF needs to set out more clearly its role in the PRS approach in each country, based on the IMF's core mandate in macroeconomic and related structural policy issues. Many Directors also supported a more active role for the IMF in the public debate on macroeconomic policy design and implementation. Where PRSPs are not yet operationally viable, the IMF should not insist on immediate tight alignment between the PRSP and PRGF-supported program. Instead, IMF staff should work with these members to strengthen their macroeconomic frameworks in PRSPs. However, increased flexibility should not imply delinking the PRGF from the PRSP, and the IMF would still seek to apply the PRSP principles in its program work.	Additional work on the PRSP process will be done in the context of the Managing Director's Report on the IMF's Medium-Term Strategy and a planned paper on the role of the IMF in the PRS process and in donor collaboration will be prepared. Board scrutiny has been simplified, as PRS documents and corresponding JSANs will no longer be put automatically on the Board agenda. Instead, they will be issued for information and discussed only at an Executive Director's request. Where PRS documents do not provide an operational strategy, this can be set out in the context of PRGF-supported programs. Where the strategy has weaknesses that are critical to the success of PRGF-supported programs, the LOI/MEFP and staff report for the PRGF request or review is expected to set out how the weaknesses have been addressed. A separate JSAN is no longer required for PRSP preparation status reports; instead, a brief discussion of the status report is included in the PRGF staff report.
5. Strengthen prioritization and accountability on what the IMF itself is supposed to deliver within the broader partnership framework, built around the priorities emerging from the PRS process, and ensure resources match commitments.	Directors welcomed the emphasis on better defining priorities for the IMF's work in low-income countries and indicated that the prioritization of budget resources must be guided by the IMF's overall mandate. They called for a careful assessment of the resource implications of adapting the IMF's role along the lines of the report's recommendations.	See response to number 4 above.
6. The IMF should encourage a strengthening of the framework for establishing the external resources envelope as part of the PRS approach.	Directors indicated that the IMF should play a supportive role with donors and low-income members to help ensure adequate provision of aid to achieve the MDGs. In this regard, the IMF needs to consider how its signals can be clear and useful to its members.	The IMF and World Bank are working with a number of countries to develop alternative macroeconomic framework that reflect the larger amount of aid needed to meet MDGs. The Board has established a new policy support instrument and an exogenous shock facility (under the PRGF) for low-income countries that may not need a PRGF arrangement but seek IMF assessment and endorsement of their economic policies.

1/ This column summarizes the reaction of the Executive Board on each recommendation as reported in the Acting Chairman's Summing Up of the July 21, 2004 Board meeting. Although care has been taken to ensure accuracy, readers are invited to refer to the full text of the summary of the discussion, which is included in the published version of the report and can be accessed on the IEO website at www.imf.org/External/NP/ieo/2004/prspprgf/eng/index.htm.

EVALUATION OF THE ROLE OF THE IMF IN ARGENTINA, 1991–2001: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Crisis Management		
The IMF should have a contingency strategy from the outset of a crisis, including in particular "stop-loss rules"—that is, a set of criteria to determine if the initial strategy is working and to guide the decision on when a change in approach is needed.	Most Directors viewed contingency planning as useful, but many noted that in a crisis or precrisis setting, it is not always possible to assess the various contingencies that might occur. Concern was also expressed that any indication that the IMF was developing contingent strategies could undermine confidence in the program. As regards specific stop-loss rules, while some Directors supported their consideration, most felt that defining and implementing such rules would be difficult or impractical.	No consensus emerged in the Board meeting.
Where the sustainability of debt or the exchange rate is in question, the IMF should indicate that its support is conditional upon a meaningful shift in the country's policy while remaining actively engaged to foster such a shift. High priority should be given to defining the role of the IMF when a country seeking exceptional access has a solvency problem.	Directors agreed with the IEO's recommendation. At the same time, they noted that assessing exchange rate or debt sustainability will necessarily entail judgment, and it is essential that the Board be provided with up-to-date and comprehensive information and analysis. Steps have already been taken since the Argentine crisis to strengthen the basis on which debt and exchange rate sustainability assessments are made. Directors indicated that they looked forward to an opportunity to assess whether further changes may be needed.	In June 2002, the Board adopted a framework for more objective and standardized debt sustainability analysis; refinements to this framework were endorsed by the Board in July 2003. Debt sustainability analyses are now regularly included in staff reports for Article IV consultations and use of IMF resources. They play a central role in considering exceptional access and in the Evian approach of Paris Club creditors. Some progress is being made in the Board to define the role of the IMF in solvency problem cases, with emphasis on the use of Collective Action Clauses.
Surveillance		
Medium-term exchange rate and debt sustainability should form the core focus of IMF surveillance. To fulfill these objectives (which are already current policy), the IMF needs to improve tools for assessing the equilibrium real exchange rate that are more forward-looking and rely on a variety of criteria, examine debt profiles from the perspective of "debt intolerance," and take a longer-term perspective on vulnerabilities that could surface over the medium term	Directors concurred with the IEO's recommendation that medium-term exchange rate and debt sustainability should form the core focus of IMF surveillance. They cautioned that finding an appropriate operational measure of exchange rate sustainability would be difficult, but a few suggested that the development of such a measure by the staff should be a priority. Directors saw a continued need for greater candor in the treatment of exchange rate policy in the context of Article IV discussions. In order to avoid triggering a potentially destabilizing market reaction, some suggested that the scope for establishing procedures for handling sensitive topics during surveillance exercises should be explored by staff. As to debt sustainability, recent events have led to a reassessment of what level of debt is sustainable for emerging market countries, which is already reflected in the IMF's work. Directors asked staff to continue to sharpen its analytical tools, and a few called for examining ways to strengthen the organization and independence of debt sustainability analysis work.	Upon completing the 2004 Biennial Review of Surveillance, the Executive Board established sharper exchange rate surveillance and improved analysis of debt sustainability as priority objectives. Since then, both areas have been receiving special emphasis in staff guidance, training, research and in the internal review process.

Evaluation of the Role of the IMF in Argentina, 1991–2001: Recommendations, Board Response, and Subsequent Follow-Up (concluded)

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Program Relationship		
The IMF should refrain from entering or maintaining a program relationship with a member country (in the form of a precautionary arrangement) when there is no immediate balance of payments need and there are serious political obstacles to needed policy adjustment or structural reform.	Directors noted the possible risks associated with precautionary IMF arrangements, especially where there are serious political obstacles to needed policies and reforms, but most did not support the implication that the IMF should not enter into a program relationship with a member country when there is no immediate balance of payments need. They reiterated the value of precautionary arrangements as an important tool for supporting sound policies, while agreeing that there is a need to ensure that program standards and requirements are the same as those for all other arrangements.	The Board did not support the recommendation, so no explicit follow-up is expected. However, in response to the expiration of the Contingent Credit Line, there is an ongoing debate on the need for, and desirability of, a new policy that would clarify the use of exceptional access under precautionary arrangements. Many Directors support the existing IMF policies as adequate.
Exceptional access should entail a presumption of close cooperation between the authorities and the IMF, and special incentives to forge such close collaboration should be adopted, including mandatory disclosure to the Executive Board of any critical issue or information that the authorities refuse to discuss with (or disclose to) staff or management.	Directors stressed that all cases of the use of IMF resources, particularly cases of exceptional access, should entail a presumption of close cooperation. Many Directors agreed that there should be a requirement of mandatory disclosure to the Board of any critical issues which the authorities refuse to discuss.	
The Decision-making Process		
In order to strengthen the role of the Executive Board, procedures should be adopted to encourage (i) effective Board oversight of decisions under management's purview; (ii) provision of candid and full information to the Board on all issues relevant to decision making; and (iii) open exchanges of views between management and the Board on all topics, including the most sensitive ones.	Directors noted that the procedures for exceptional access adopted since the Argentine crisis have generally worked to strengthen the Board's involvement and ensure that decisions to continue program engagement under exceptional access are adequately informed. A number of Directors, however, saw a need for further discussion of approaches to strengthen the role of the Board. Further efforts to enhance decision making by the Board would include improvements in the provision of full information on all relevant issues and open exchanges of views between management and the Board on all topics, including the most sensitive ones.	

1/ This column summarizes the reaction of the Executive Board on each recommendation as reported in the summing up by the Chair. Although care has been taken to ensure accuracy, readers are invited to refer to the full text of the summary of the discussion which is included in the published version of the report and can be accessed from the IEO website (www.imf.org/ieo).

2/ The description of follow-up is intended to provide a factual indication of any additional steps taken since the Board discussion. It is not intended to be an evaluation of any follow-up by management or the Board.

EVALUATION OF IMF TECHNICAL ASSISTANCE

IEO Recommendations	Executive Board Response	Task Force Recommendations 1/	Follow-Up 2/
1. Prioritization and resource allocation The IMF should develop a medium-term country policy framework for setting TA priorities, incorporating country-specific strategic directions and linked to more systematic assessments of factors underlying past performance.	Directors endorsed this recommendation and generally supported the managerial approaches suggested for carrying it forward. In particular, most Directors agreed that in low-income countries, the PRSP should increasingly serve as a vehicle for identifying medium-term TA needs and improving coordination among agencies, although in a number of cases, the focus of PRSPs will need to be sharpened to carry out this role effectively. In other countries, Directors stressed the importance of developing country-centered frameworks for identifying TA needs and noted that a variety of approaches—possibly including greater use of Article IV consultations to assess needs—may be appropriate.	Short *TA Country Strategy Notes* (TACSNs) should be prepared for "intensive IMF TA users" and systemically important TA countries. With a strategic perspective developed in their surveillance or UFR activities, area departments would identify the issues/problems to be addressed by TA. TACSNs would present the IMF's TA strategy to the authorities, and seek their input into that strategy. TACSNs should provide area and functional departments with a solid information base to further their dialogue on TA prioritization decisions. In view of the possible significant resource implications of this proposal and an inconclusive earlier experience with Technical Consultations, the proposal would be launched on a pilot basis.	Area departments already include TA monitoring on their Resident Representative terms of reference when applicable. 3/ TACSN pilot has been completed in April 2006. An evaluation of experience with the TACSN pilot is currently ongoing, with a view to preparing a possible guidance note on the form and content for a next set of TACSNs under guidance from the Technical Assistance (TA) Subcommittee of the MTS Committee on Capacity Building (CCB).
2. Tracking progress and reasons for shortfalls The IMF should develop more systematic approaches to track progress on major TA activities and to identify reasons behind major shortfalls.	Directors supported the recommendation that at the outset of major TA activities, staff and authorities should agree on measurable indicators of progress covering all major stages of the TA life cycle. Better tracking includes careful explanation of shortfalls in execution, and candid staff reporting on obstacles to progress. However, on these endeavors staff should avoid imposing conditions on members without their consent. While supporting the view that implementation records should be an important guide in weighing TA requests, a number of Directors cautioned against using tracking indicators mechanistically for TA resource allocations.	The Task Force notes the IEO's view on the TA Information Management System (TAIMS) that was being developed as "an opportunity to systematically improve tracking and monitoring of TA on a IMF-wide basis," and a "vehicle through which enhanced monitoring practices become unified and more transparent across the institution." Agreeing with that view, it notes that TAIMS is expected to systematically include clear ex ante set of progress indicators and identified risk factors, to record outputs and other measurable indicators, and to provide for their monitoring.	In the context of the Task Force on Performance Indicators, staff is seeking to identify different types of TA outputs for the purpose of tracking and monitoring performance. TAIMS now generates monthly mission activity reports. TAIMS is being extended to the IMF's regional TA centers, and further work is ongoing on enhancing TAIMS as a monitoring tool. In particular, the Working Group on Monitoring and Evaluation (WGME) has been reconvened to explore and pursue the next steps in TAIMS's development.

Evaluation of IMF Technical Assistance (continued)

IEO Recommendations	Executive Board Response	Task Force Recommendations 1/	Follow-Up 2/
3. Interaction with authorities and local experts Greater involvement by the authorities and counterparts in the design of TA activities and arrangements for follow-up should be emphasized as a signal of ownership and commitment.	Directors concurred that greater involvement and ownership by the recipient authorities and discussion of options are crucial to greater TA effectiveness. They welcomed the proposals for more participation by country authorities in drawing up terms of reference (TORs) while systematically seeking their tangible commitments to the contemplated TA strategy or advice early on. However, a number of Directors cautioned that these indications of commitment should not be treated as conditionality for access to TA.	TA departments should further strengthen the dialogue with country authorities when drafting TORs for short- and long-term experts, and systematically seek their inputs. To enhance the likelihood of implementation, foster lessons learning, and disseminate best practices, those departments should systematically seek the authorities' consent to disseminate TA reports among the country's technical staff, IMF Executive Board, and selected donors. Broader circulation and availability of the TA reports could help in building consensus around proposed reforms and strengthen the authorities' resolve to follow up on recommendations.	TA departments have made efforts to enhance the dialogue with the authorities, including efforts to clearly lay out the authorities' and TA departments' expectations for TA operations. Actions suggested by the Task Force are being implemented by all departments. The preparation of TACSNs, in consultation with country authorities, would also contribute to the fulfillment of this objective.
4. Enhancing identification of options Stronger efforts should be made by TA experts to identify options and discuss alternatives with local officials prior to drafting TA recommendations.		When relevant, TA reports should record discussions with the authorities on alternative policy options, the considerations leading to them, and when there were differences of views summarize the authorities' views on key issues and recommendations.	Actions recommended by the Task Force are being implemented by TA departments. A department reports the adoption of practices whereby authorities are engaged in discussions of preliminary findings and alternative responses prior to drafting reports.
5. Ex post evaluations The program of ex post evaluations of TA should be widened and more systematic procedures for disseminating lessons put in place.	Directors highlighted the importance of ensuring that the scope of ex-post evaluations be carefully considered and integrated into a broader strategy to make TA delivery more effective. They concurred that external evaluations are a useful tool to enhance accountability and provide a fresh perspective, and that the Office of Technical Assistance Management (OTM), in collaboration with other departments, should continue to prepare and update its program of ex post evaluations and to assess shifts in TA demands across subject areas.	For larger TA projects, it is recommended that functional departments produce standardized self-assessments within three months of the conclusion of the project and include them in TAIMS. These self-assessments could be used as input to institutional lesson-learning and for ex post evaluations. To assist in this effort, it is proposed that OTM manage a TA self-assessment/evaluation knowledge base, which could be incorporated into future TA and made available to all IMF staff to maximize its potential benefits.	As a first step to designing a standardized data base on evaluations, TA departments have listed their existing evaluation practices and completed evaluations. The IMF-wide TA evaluation program has been completed for 2006, and the respective Board papers issued (http://www.imf.org/external/np/pp/eng/2006/071206.htm).

EVALUATION OF IMF TECHNICAL ASSISTANCE (CONCLUDED)

IEO Recommendations	Executive Board Response	Task Force Recommendations 1/	Follow-Up
6. Strategic decisions and tradeoffs The prioritization filters should be discontinued or replaced by ones that would more effectively guide TA allocation. Either course of action involves strategic decisions on trade-offs that need to be taken explicitly.	While Directors concurred that the case for discontinuing the current filters was strong, several of them observed that elements of this approach might usefully be preserved. TA resources prioritization should flow from a shared vision of the IMF's overall medium-term objectives—reflecting its core competencies—while at the same time retaining the flexibility to respond to the urgent needs of members. Directors agreed that the IEO's recommendations would entail more staff-intensive approaches to providing TA, including greater collaboration with country authorities and other TA providers. Going forward, Directors welcomed management's proposal to task staff to make concrete proposals on how to implement the IEO recommendations, taking into account budgetary costs, and implications for work practices and TA delivery, and looked forward to future discussion of these proposals, including on prioritization, before their implementation.	It is recommended that the current set of prioritization filters—deemed ineffective—be discontinued as the proposed remedial actions encompass the key ingredients for an effective prioritization of TA resources. If fully implemented, they would form a basic accountability framework for all the stages of the TA life cycle—prioritization, delivery, and monitoring and evaluation—against which the effectiveness of IMF TA can be gauged. To make it viable however a number of management and organizational challenges must be overcome, while its linkage to the efficient allocation of TA resources—the budget perspective—needs to be developed. The provision of adequate incentives for staff to implement the proposals, in particular for area department staff and resident representatives is critical. It is important that these proposals also feed into mechanisms that result in an efficient allocation of TA resources across countries, sectors, and policy initiatives on an evolving basis. Thus beyond the annual exercise, resource allocations for TA through the Medium Term Budget Framework will need to be informed by strategic decisions, which in turn, will require that emerging trends across departments be identified in a timely way.	Prioritization filters were discontinued. In their place, the TA Subcommittee has recommended a closer integration of the RAPs with the budgetary processes of both functional and area departments. To that end, and given the nexus between the RAP, TACSNs, and TA budgets, the TA Subcommittee has decided to set up a Working Group on Technical Assistance Resource Planning. The overall remit of the working group is to make recommendations with a view to improving procedures for allocating TA resources in a collaborative manner that is consistent with the strategic objectives of the IMF and country authorities. It is expected that the working group will present its initial findings and recommendations to the TA Subcommittee by the end of October 2006.

1/ The Task Force was created by management on March 31, 2005 in response to the Executive Board discussion of the IEO's evaluation. Their report was discussed by the Executive Board on July 27, 2005.

2/ The description of follow-up is intended to provide a factual indication of any additional steps taken since the Board discussion of the evaluation report. It is not intended to be an evaluation of any follow-up by management or the Executive Board. Where staff internal assessments have been made of relevant issues, these are reported but have not been subject to any independent confirmation by the IEO.

3/ Terms of Reference for Resident Representatives in countries which are major TA recipients should list among their responsibilities an active involvement on TA implementation, follow-up TA activities by other providers in areas of interest to the IMF, while coordinating activities where those providers are receptive to this approach.

EVALUATION OF THE IMF'S APPROACH TO CAPITAL ACCOUNT LIBERALIZATION

IEO recommendations	Executive Board response 1/	Follow-Up 2/
Recommendation 1: There is a need for more clarity on the IMF's approach to capital account issues: • The place of capital account issues in IMF surveillance could be clarified. • The IMF could sharpen its advice on capital account issues, based on solid analysis of the particular situation and risks facing specific countries. • The Executive Board could issue a statement clarifying the common elements of agreement on capital account liberalization.	Some Directors saw merit in further clarifying the scope of IMF surveillance to recognize explicitly the central importance of capital account policies; Directors also saw scope for sharpening the IMF's advice on capital account issues, urging the staff to base its policy advice on solid analysis of individual country situations. However, a variety of views were expressed on "the merit of an Executive Board statement clarifying the elements of agreement on capital account issues." Directors noted that they would have an opportunity to come back to this issue in the context of the IMF's ongoing strategic review.	Staff has been working on multiple research projects on various dimensions of capital account liberalization. RES has recently produced a comprehensive study providing a unified conceptual framework to organize the vast literature on the benefits and costs of financial globalization (IMF WP/06/189). In addition, research has been underway examining macroeconomic policies which could help developing economies effectively manage financial globalization. Staff initiated further analytical work, with a special focus on the interaction of prudential measures and capital controls that updates the integrated approach for the sequencing of capital account liberalization. A paper was presented to the Board in July 2006 which analyzed how countries can use domestic policies to reduce their vulnerability to shocks and, in particular, to sudden stops in capital flows or to external debt crises (Country Insurance: The Role of Domestic Policies, http://www.imf.org/external/np/pp/eng/2006/061906.pdf).
Recommendation 2: The IMF's analysis and surveillance should give greater attention to the supply-side factors of international capital flows and what can be done to minimize the volatility of capital movements.	Directors welcomed the various initiatives under way in the IMF to strengthen research, analysis, and surveillance of the supply side of capital flows, and encouraged the staff to continue to build on the work already being undertaken at the IMF in order to further its understanding of supply-side factors and their operational and policy implications.	

1/ This column summarizes the reaction of the Executive Board on each recommendations as reported in the Summing Up by the Chairman of the May 11, 2005 Board meeting. Although care has been taken to ensure accuracy, readers are invited to refer to the full text of the summary of the discussion, which is included in the published version of the report and can be accessed from the IEO website (http://www.imf.org/External/NP/ieo/2005/cal/eng/index.htm).

2/ The description of follow-up is intended to provide a factual indication of any additional steps taken since the Board discussion of the evaluation report. It is not intended to be an evaluation of any follow-up by management or the Executive Board. Where staff internal assessments have been made of relevant issues, these are reported but have not been subject to any independent confirmation by the IEO.

EVALUATION OF THE IMF SUPPORT TO JORDAN 1989–2004: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP

IEO Recommendation 1/	Executive Board Response 2/	Follow-Up 3/
Broad lessons suggested by the IMF experience in Jordan		
The underlying rationale for key program design elements should be explained clearly in Board papers. In particular, judgments on the magnitude and composition of targeted adjustment need to be grounded in an explicit assessment of external and public debt sustainability over the medium term.	Many Directors agreed that the Jordanian experience reinforces the need for Board papers to provide clearly the underlying rationale for key elements of program design. They also supported the IEO's call for greater candor in staff report assessments, especially of the risks to the program and recommendations on how best to mitigate and manage them.	Jordan has been under Post Program Monitoring (PPM) since July 2004. The macroeconomic framework and adjustment profile is based on the fiscal and external debt sustainability analysis. Staff reports under PPM have become more candid (see in particular EBS/05/154).
In certain circumstances, structural conditionality can have significant value added in terms of encouraging and monitoring progress on reforms. However, underlying issues such as large and abrupt surges in grants require that programs be set in an explicitly longer-term perspective. Timetables need to be designed carefully, taking account of the political economy situation, especially when legislative action is involved.	Directors agreed with the report's overall assessment: Jordan's long engagement in IMF-supported programs helped the authorities address macroeconomic stabilization challenges successfully, although structural rigidities remain to be addressed. While agreeing that structural conditionality had been well designed, many Directors also pointed to the lessons for the timing of these conditions offered by the Jordanian experience. In particular, they noted the importance of ambitious but realistic timetables that take into account a country's implementation capacity as well as the prevailing political and social environment.	
The IMF's program involvement would have been more effective if programs had given greater emphasis at an earlier stage to the formulation of key institutional reforms in the fiscal area.	Directors considered that a longer-term perspective, with greater emphasis at an earlier stage on the formulation of key institutional reforms in the fiscal area, would have increased the effectiveness of IMF-supported programs	
A wider dissemination of IMF TA reports would have contributed to more informed public discourse and shed light on the rationale for IMF policy advice on key issues.	Directors concurred with the IEO's lesson that a wider dissemination of IMF TA reports could have contributed to more informed public discourse and shed light on the IMF policy advice on key issues. At the same time, Directors noted that decisions on disseminating such reports are ones for the authorities to take.	
The IMF's future role in Jordan		
Help Jordan manage the projected decline in grants in a manner that preserves the gains made in the areas of macroeconomic stability and longer-term fiscal sustainability. This will be done by (a) helping the authorities design a macroeconomic framework that will achieve a smooth transition and (b) focusing on helping to design strategies to tackle Jordan's key remaining fiscal rigidities, including exploring alternative policy options to achieve the necessary structural reforms in the fiscal area.	The Board shared the view that Jordan still faces the challenges of adjusting to a sharply lower level of foreign grants and reducing fiscal rigidities. Most Directors noted that these challenges would have been less daunting had more progress been made on critical reforms during Jordan's longer-term program engagement.	The authorities have made progress in formulating their own medium-term macroeconomic adjustment strategy. Going forward, the staff remains in close consultation with the authorities through surveillance and the provision of technical assistance. The focus of future consultations will be on helping the authorities design a macro-fiscal framework that would preserve macroeconomic stability and ensure debt sustainability in the environment of high oil prices and declining grants, and to reduce the remaining fiscal rigidities by improving tax administration and reforming the system of fuel subsidies.

1/ The Jordan Evaluation report made no explicit recommendations, presenting instead a number of lessons arising from IMF experience in Jordan.

2/ This column summarizes the reaction of the Executive Board on the lessons presented in the Jordan evaluation as reported in the Summing Up by the Acting Chair. Readers are invited to refer to the full text of the summary of the discussion, which is included in the published version of the report and can be accessed on the IEO website (www.imf.org/external/NP/ieo/2005/jor/eng/pdf/sumup.pdf).

3/ There was no explicit follow-up strategy. However, Jordan's Ex-Post Assessment was done about the same time as IEO's Evaluation of IMF support to Jordan (and presented to the Executive Board on the same day); there was cooperation between the teams carrying out these evaluations.

EVALUATION OF THE FINANCIAL SECTOR ASSESSMENT PROGRAM: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Incentives for participation, clarifying priorities, and strengthening the links with surveillance		
Recommendation 1. The IMF Board and management should refine the criteria for setting priorities on IMF resource inputs into financial sector surveillance, including the FSAP. Based on these priorities, IMF staff should indicate, as part of its medium-term planning, what components are needed for strengthening financial sector surveillance in each country, drawing upon a range of possible modalities. These strategies would form the basis for more explicit accountability on results.	While some did not see sufficient evidence that current mechanisms are inadequate, many Directors agreed on the need for clearer guidance—including on the trade-off between assessments of vulnerability and development issues—as part of a medium-term strategy aimed at efficient resource allocation in line with the IMF's core mandate.	Consideration being given to the three pillars of recommendations in the context of ongoing work on the Medium Term Strategy and a task force on integration of regular and financial sector surveillance. The country prioritization process has been strengthened by distinguishing more clearly between the intrinsic country priorities—in a program that over time should cover all countries—and the likely work program that is affected by authorities willingness to participate. On a region-wide basis, FSAP prioritization is carried out every 6 months through consultations between MCM and area departments and through the FSLC, The modalities of financial sector surveillance in individual countries, including an initial assessment or FSAP update, are assessed in Article IV briefing papers and staff reports, and other country-specific discussions between MCM and area departments.
Recommendation 2. To strengthen incentives and drawing upon these country-specific plans, IMF management should clearly signal to the Board those countries that it sees as the highest priorities for FSAPs and Updates, irrespective of whether these countries have volunteered. These lists should be the basis for periodic discussions by the Board of country-specific priorities.	Most Directors agreed with the IEO proposal that, to better align FSAP coverage with the needs of surveillance, management should indicate to the Board which countries it considers the highest priorities for FSAP assessments and updates. Annual reporting on participation could provide useful information to guide discussion of priorities.	The IMF-Bank FSLC has already identified countries that should be given the highest priority under the FSAP, following the general criteria approved by the IMF and Bank Boards and based on inputs from staff of both institutions. Staff plan to use a two-pronged approach, using (i) the regular Article IV process to signal a need for intensified financial sector surveillance and to indicate the need to explicitly recommend in the Article IV report an initial FSAP or FSAP update in priority cases, and (ii) providing more frequent information on FSAP participation. Staff plan to use the annual report on FSAP participation (introduced in the 2005 Board review of the FSAP) to provide the Executive Board with overall information on program coverage, including information on the relative size of systems covered and not covered. The first such report was sent to management and the Board in June 2006.

EVALUATION OF THE FINANCIAL SECTOR ASSESSMENT PROGRAM: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONTINUED)

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Recommendation 3. Strengthen the links between the FSAP and surveillance by mainstreaming FSAPs and follow-up work into regular surveillance activities.	Directors concurred with the recommendation to strengthen links between FSAPs and surveillance. They underscored the need to follow up on key vulnerabilities and gaps and integrate such issues into Article IV surveillance reports. Directors stressed that in cases where financial stability issues, including any potential global repercussions, are judged to be of high importance, they should be a major focus of Article IV consultations.	Following the MTS, area departments are to identify a senior staff member who will be responsible for the departments' financial sector surveillance (FSS) and coordination of the FSS work program with MCM. FSS training will be provided to staff at all levels as needed. Moreover, the introduction (by the MTS) of country-specific 3-year surveillance agendas (SAs) should help ensure adequate follow through of financial sector surveillance priorities. A Financial Sector Steering Group including representatives of area and relevant functional departments has been set up by the managing director to ensure high level coordination of the work of all departments involved in FSS. Separately, an ad hoc internal Financial Sector Task Force is preparing specific recommendations on how to integrate the analysis of financial sector issues into bilateral surveillance. The internal review process of FSAP related documents and Article IV reports is being strengthened to ensure that the Executive Summary summarizes the main macro-relevant findings using candid language, the FSSAs clearly highlight and summarize macro relevant findings, and that these findings are adequately reflected and incorporated in the analysis of the Article IV report.
Improving the quality and impact of the FSAP and organizational changes		
Recommendation 4. Implement steps to improve further the quality of the FSAP and strengthen its impact.	Directors encouraged the staff to follow up on IEO recommendations to improve further the quality of FSAPs and strengthen their impact. They noted that recommendations should be clearly prioritized and the potential consequences candidly discussed. Directors emphasized in particular the importance of treating financial sector and cross-border linkages more systematically in FSAP analysis.	FSAP procedures are being revised to stress that (i) recommendations need to be candidly discussed and clearly prioritized, given the authorities' capacity constraints (ii) missions should cover all major risks, including those that may be politically sensitive. In cases where adequate data are lacking, potential major risks should nevertheless be explicitly identified and limitations transparently discussed. The revised procedures will also stress the need to have more informative and candid discussions on methodological and data limitations in FSSAs. Staff is developing the stress testing methodology and establishing "minimum standards" for stress tests, to ensure that stress test methodologies are applied more consistently across countries. Work on regional financial sector assessments and cross-border issues has been stepped up and off-shore financial center (OFC) reports are now expected to include a section on cross-border cooperation and information exchange. A program is being initiated to improve standards assessments, including the establishment of a core set of experienced assessors; the role of cooperating institutions and standard setters; and the review process and quality control. An internal review was conducted to evaluate BCP, IOSCO, and IAIS assessments in order to improve the quality and consistency of the assessments. Staff will participate in a December 2006 IOSCO meeting to improve standards assessments. Regular courses and seminars are offered to IMF staff on the use of financial sector indicators, stress testing and relevant financial sector issues to enhance practical experience and expertise.

EVALUATION OF THE FINANCIAL SECTOR ASSESSMENT PROGRAM: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP (CONCLUDED)

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Recommendation 5. Introduce changes in the organization of IMF mission activities to utilize scarce financial sector technical expertise (especially in MFD and ICM) more effectively in the surveillance process.	Many Directors welcomed the IEO's recommendation to introduce changes in the organization of IMF mission activities to utilize more effectively scarce financial sector expertise within the IMF. Directors noted that this will be considered in the broader context of improving financial sector surveillance, as part of the medium-term strategic review.	The modalities to do this are being assessed as part of the MTS and also in the assessment of the pilot project on financial sector surveillance.
Joint IMF-World Bank Nature of the FSAP		
Recommendation 6. Maintain the current joint approach, but clarify further the distinctive contributions the IMF and Bank can make, with the IMF taking the lead where significant domestic or global stability issues are present, and the Bank taking the lead where financial sector development issues are more paramount. Such clarity should include a clear delineation of primary responsibilities for setting priorities (and contributing resources).	Directors were in broad agreement with the recommendations regarding Bank-IMF collaboration. They concurred that the current joint approach, including the central role for the Bank-IMF FSLC, should be maintained. At the same time, further efforts should be made to take full advantage of the distinctive contributions that the two institutions can make—with the IMF focusing on stability issues and the Bank on financial sector development and institution building.	The delineation of responsibilities between the Bank and the IMF will be addressed more fully by the Bank-IMF Collaboration Task Force. Staff will step up its efforts to ensure at the scoping stage that the Bank indeed takes the lead regarding financial sector development issues.
Recommendation 7. The IMF, in conjunction with the World Bank and other technical assistance providers, should seek to establish a clearer framework for coordinating follow-up capacity-building technical assistance activities, based on the country's own action plans.	Directors concurred that there is room to improve the coordination of FSAP-related technical assistance activities, based on the country's own action plan. At the same time, Directors cautioned against overburdening the FSAP with additional expectations regarding the technical assistance needs.	Staff has organized post-FSAP TA meetings in some recent cases. Staff will include in the transmittal letter for the FSAP package, when appropriate, a suggestion that a follow-up meeting or "providers forum" on technical assistance be organized. The decision on whether to include such a suggestion will be based on discussion with the area departments and the World Bank, and following the Board's guidance not to overburden the FSAP with additional expectations and excessively formal approaches to follow-up.

1/ This column summarizes the reaction of the Executive Board on each recommendation as reported in the summing up by the Chair. Although care has been taken to ensure accuracy, readers are invited to refer to the full text of the summary of the discussion which is included in the published version of the report and can be accessed from the IEO website (www.imf.org/ieo).

2/ The description of follow-up is intended to provide a factual indication of any additional steps taken since the Board discussion. It is not intended to be an evaluation of any follow-up by management or the Board.

EVALUATION OF THE IMF'S MULTILATERAL SURVEILLANCE: RECOMMENDATIONS, BOARD RESPONSE, AND SUBSEQUENT FOLLOW-UP

IEO Recommendation	Executive Board Response 1/	Follow-Up 2/
Recommendation 1. Strengthen the IMF's role at the center of a more robust global peer review system by establishing a more proactive engagement with relevant intergovernmental groups.	Most Directors concurred that, while the Executive Board and the IMFC remain the most appropriate forums for discussing policy spillovers and possible responses, the IMF should also participate more actively in other forums—such as, but not limited to, the G-7 and the G-20—which provide opportunities for a frank exchange of views on multilateral issues. Directors noted that multilateral surveillance would have a larger effect on the global policy debate if they were better targeted to their core audiences, streamlined, and focused on key issues. Directors agreed that it would be beneficial to clarify the operational goals of multilateral surveillance, but were not persuaded about the need for broad organizational changes. Priority should be given to strengthening the integration between multilateral and bilateral surveillance, particularly for countries that have an impact on global financial stability.	A new multilateral consultation process has commenced, with key players involved in the solution of issues of shared global or regional interest.
Recommendation 2. Enhance the roles of the Executive Board and the IMFC in multilateral surveillance.		
Recommendation 3. Streamline and better focus the products of multilateral surveillance, present shorter and clearer messages, and deliver them more strategically to target groups.		The WEO is being reconfigured to highlight key cross-country messages and strengthen risk analysis. Work is ongoing to focus post-WEO outreach on issues of particular concern in specific regions.
Recommendation 4. Define more clearly the goals of multilateral surveillance and the mechanisms to achieve them. Particular effort should also go into better integrating multilateral perspectives into bilateral surveillance.		Consistent with the Medium-Term Strategy (MTS), Article IV reports for systemically important countries will be expected to include analysis and discussion of regional or global spillover effects, and all Article IV consultations are expected to make a greater use of cross-country analysis and to bring to bear other countries' experience in addressing similar problems. To aid integration of bilateral and multilateral surveillance the results of the WEO will be presented to staff in an internal seminar.

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